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# The Emerging Fourth Sector

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# Abstract

The Fourth Sector is a new phenomenon related to dual social and financial value creation, until now not clearly defined with crisp sectoral boundaries and an operationalized definition. The phenomenon is getting increased attention in media, conferences, business schools and by organizations all over the world, and this study intends to explain the macro-environmental changes that led to the rise of the fourth sector, describe new trends of social value creation in the private sector and financial value creation in the nonprofit sector – and thereby also find that there is a convergence of sectors towards a new hybrid intersection of dual social and financial value creation – sometimes referred to as the fourth sector. The existing definitions will be criticized, and the fourth sector will be redefined with a new, more operationalized definition.

In addition, a strategic analysis of two fourth sector companies – Me to We Style and God El – will be conducted. This analysis will focus specifically on the internal analysis of these companies, analyzing whether the fourth sector business model leads to any competitive advantages/disadvantages. All other things will be isolated from this analysis, and an external analysis will not be relevant here, since the fourth sector business model will not influence the external competitive environment in these cases. Relevant findings are indications that fourth sector companies (here defined by God El and Me to We Style) can have competitive advantages in their fourth sector business model, in their customer relations, in their employee relations and especially in their relationships with their suppliers and other alliances, where they are able to really leverage the business model, saving cost for the company. It is unclear whether access to capital might become a competitive disadvantage for fourth sector companies over time – it is not for these two fourth sector start-ups analyzed here.

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# Table of Contents

Abstract .....	2
Acknowledgements .....	3
Table of Contents .....	4
Figures Overview .....	7
Tables Overview .....	7
 Chapter 1 - Introduction .....	8
1.1 Introducing the Fourth Sector .....	8
1.1.1 Capitalism Reformed .....	8
1.1.2 Blurring sectors and hybrid organizations .....	9
1.2 Research Questions and Purpose of Dissertation .....	10
1.3 Structure .....	12
 Chapter 2 – Setting the stage .....	13
Macro-changes in Society .....	14
2.1 The fall of communism .....	14
2.2 The dominance of the MNC .....	15
2.3 An era of globalization and collaboration .....	17
2.5 Sustainable Development .....	18
2.6 The “failure” of old solutions .....	20
2.6.1 The Bottom of the Pyramid .....	23
Micro-changes in society .....	24
2.7 The Postmaterialistic Era .....	24
2.8 New economic theories of human motivation .....	25
2.9 Chapter Analysis .....	29
 Chapter 3 – Trends and concepts related to social value creation in the private sector .....	33
3.1.1 The Shareholder Perspective – Milton Friedman’s view on CSR .....	36
3.1.2 The Stakeholder Perspective – Edward Freeman’s view on CSR .....	37
3.1.3 Strategy and Society – CSR and competitive advantage .....	39
3.1.4 Corporate Social Initiatives .....	42
3.1.5 Corporate Citizenship .....	43
3.1.6 Corporate Philanthropy .....	45

3.1.7 Criticism of Corporate Social Responsibility .....	46
3.2 Cause Related Marketing (CRM) .....	47
3.2.1 Concerns with CRM .....	49
3.3 The Triple Bottom Line .....	50
3.3.1 Criticism of the triple bottom line.....	52
 Chapter 4 – Trends and concepts related to financial value creation in the social sector .....	54
4.1 Social entrepreneurship.....	54
4.1.1 Criticism of social entrepreneurship .....	57
4.2 Social business.....	58
4.2.1 Criticism of social business .....	60
 Chapter 5 – Converging Sectors - Dual Value Creation.....	61
5.1 Hybrid companies, for-benefits and the fourth sector .....	63
5.1.1 Kim Alter’s Hybrid Spectrum.....	63
5.1.2 Existing definitions of the fourth sector.....	67
 Chapter 6 – A New Definition of the Fourth Sector.....	70
6.1 Criticism of definitions in chapters 3, 4 and 5 .....	70
6.1.1 Corporate Social Responsibility, CRM and the Triple Bottom Line.....	70
6.1.2 Social Entrepreneurship and Social Business .....	71
6.1.3 Hybrid Organizations and the “blurring sectoral boundaries” .....	72
6.2 Defining the Fourth Sector.....	73
6.2.1 The Fourth Sector Matrix.....	76
6.2.2 The Sector Continuum .....	77
6.3 Clarifications.....	77
6.3.1 Revenue vs. Dividend / Profit / Ownership .....	77
6.4 What is not a Fourth Sector Company? .....	79
6.5 Examples of Fourth Sector Companies.....	80
6.6 Criticism & Issues.....	81
6.7 Chapter Conclusion.....	83

Chapter 7 – Theoretical Framework for Strategic Analysis: A Resource-Based View .....	85
7.1 Defining Competitive Advantage .....	85
7.2 Identifying Competitive Advantages .....	87
7.2.1 The EQIC-model.....	87
7.2.2 VRIO-analysis.....	89
Chapter 8 – Empirical Data & Analysis .....	91
8.1 Case Presentation .....	91
8.1.1 Me to We Style .....	91
8.1.2 God El .....	92
8.2 EQIC-analysis .....	93
8.2.1 Me to We Style .....	93
8.2.2 God El .....	95
8.3 VRIO-analysis.....	96
8.3.1 Me to We Style .....	96
8.3.2 God El .....	98
8.4 Survey Findings .....	100
8.4.1 Customers .....	100
8.4.2 Recruiting.....	100
8.4.3 Employees and Wages .....	101
8.5 Chapter Conclusion.....	102
Chapter 9 – Implications and Conclusion.....	103
Bibliography.....	105
Books .....	105
Articles.....	106
Reports & Surveys .....	107
Websites & Other.....	108
Appendices.....	109
Appendix 1 – New York Times Article.....	109
Businesses Try to Make Money and Save the World.....	109
Appendix 2 – Financial Times Article.....	117
Social enterprise - the fledgling fourth sector.....	117
Appendix 3 – God El Interview .....	120
Appendix 4 – Kavli Group Interview .....	122

## Figures Overview

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Figure 1 - A visualization of Chapter 2 .....	13
Figure 2 - The Economic Pyramid.....	22
Figure 3 - The fortune at the bottom of the pyramid (Prahalad, 2006).....	23
Figure 4 – Freeman’s original stakeholder model .....	37
Figure 5 - M. Yunus’ 4 types of social entrepreneurs.....	60
Figure 6 - Convergence of Sectors.....	62
Figure 7 - The Hybrid Spectrum.....	65
Figure 8 – Social Enterprise mission orientation.....	66
Figure 9 - Level of integration between social programs and business activities .....	66
Figure 10 - The Blurring Sectoral Boundaries (Fourth Sector Network, 1998).....	69
Figure 11 - The Fourth Sector Matrix.....	76
Figure 12 - The Sector Continuum .....	77
Figure 13 - The roots of competitive advantage (Hill & Jones, 2004) .....	86
Figure 14 - Generic building blocks of competitive advantage (Hill & Jones, 2004) .....	88

## Tables Overview

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Table 1 - Number of hits in Google .....	33
Table 2 - Definitions of Corporate Social Responsibility (CSR) .....	35
Table 3 - Definitions of Corporate Citizenship.....	44
Table 4 - Definitions and descriptions of social entrepreneurship and social entrepreneurs. (Zahra, Gedajlovic, Neubam, & Shulman, 2006) .....	57
Table 5 - Spectrum of Practitioners (Alter, 2004) .....	64
Table 6 - Examples of Fourth Sector Companies .....	80
Table 7 - The VRIO-criteria .....	90
Table 8 - The VRIO framework applied on Me to We Style.....	98
Table 9 - The VRIO framework applied on God El .....	99

# Chapter 1 - Introduction

## 1.1 Introducing the Fourth Sector

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### 1.1.1 Capitalism Reformed

When Muhammad Yunus and Grameen Bank were awarded the Nobel Peace Prize in December 2006, this was an eye-opening event to many people. The Nobel Peace Prize Committee had done something very few expected them to, but something that still felt very natural – they had awarded the Nobel Peace Prize to an economist and a bank.

In many ways this was a ground-breaking event, the recognition of business and capitalism as an enormously powerful way to fight poverty, or for that case, as a way of fighting for other good causes as well. But Dr. Yunus and Grameen Bank are not capitalists the way most people understand the concept. Muhammad Yunus represents a new breed of capitalists – a breed that interpret capitalism in a broader way than before. Dr. Yunus has described an organizational model – the social business, which acts on the premises of hard-core capitalism, but where the mission is not to enrich a few owners but create positive social change for the society in which the business operates (the social business is often owned by the people itself).

At the World Economic Forum in Davos 2008, Bill Gates also spoke up for a more humanistic version of capitalism, and he proposed to call this “creative capitalism” – a term that has caused quite a stir. The ideology calls for a new form of capitalism that works both to generate profits and solve the world’s inequities, using market forces to better address the needs of the poor. According to Gates, “disparities between the rich and the poor are greater today than ever”, and the idea of creative capitalism combines the “two great focuses of human nature -- self-interest and caring for others”. (Kinsley et al., 2008) Gates’ idea is not novel at all – merely a version of strategic corporate social responsibility.

Rooted in the same public demand for changes to the capitalistic system as pinpointed by Gates and Yunus, the catchphrase of “social entrepreneurship” is another term that is gaining



popularity. The concept gets gradually more attention by printed- and online media, conferences, business-schools and organizations. An example is former CEO and co-founder Jeff Skoll of eBay. He stepped down and sold some of his shares in the IT-giant in 1998 (worth \$2billion), and started the Skoll Foundation for Social Entrepreneurship in 1999. In 2003 the foundation launched the Skoll Centre for Social Entrepreneurship at Oxford Said Business School, and the annual Skoll World Forum around the same topic – a conference that in few years has become quite influential and frequently visited by various state leaders and Nobel Peace Prize winners.

According to Chip Feiss in a recent article in Financial Times (Feiss, 2009), nonprofit organizations have doubled in number in the US alone in the past 15 years. Feiss also says that “increased social awareness motivated people to align their investments better with their values and gave birth to socially responsible investing, which has also seen dramatic growth. In the UK, funds invested with a socially responsible focus have grown from £1bn to £764bn (\$1,260bn, €897bn) in 12 years. The opportunity for social enterprise is huge. The Monitor Group estimates that this could be a \$500bn-a-year sector within five to 10 years” (ibid).

Chip Feiss argues that “although experiencing a huge upsurge in interest and visibility globally, social enterprise is still in its nascent stages” and faces some structural challenges, the actual definition being one of them. He says that “the term “social enterprise” has been imbued with many different meanings and become associated with other catchphrases such as *sustainability*, *green* and *corporate social responsibility*”, and further defines it as “a for-profit/non-profit or hybrid business, using private investment to work on common-good social problems. (Feiss, 2009)”.

### 1.1.2 Blurring sectors and hybrid organizations

Uffe Elbæk, the creator of the Kaospilot-school in Denmark, argues that the three existing sectors experience a pressure from outside in order to change their habits (Elbæk, 2004). The consequence is that because of this pressure and new demands, the organizations in the sectors start to change towards something new and better. This leads to the rise of new organizations with different and innovative business models of *dual social and financial value creation which can be said to constitute an entirely new sector – the fourth sector (of hybrid organizations)*. According to Elbæk, the fourth sector integrates the advantages from

the three existing sectors and meets the citizens' requirements in a way that exceeds those of the private, the public and the non-profit sector.

In early May 2007, the newspaper The New York Times published an article on the Fourth Sector, as one of the first well-known media to describe the phenomenon. The article was intercepted by other media and also a lot of bloggers, who immediately started to discuss this new phenomenon. The article in NY Times stated that *"the term fourth sector derives from the fact that the participants [in the sector] are creating hybrid organizations distinct from those operating in the government, business and non-profit sectors, organizations driven by both social purpose and financial promise that fall somewhere between traditional companies and charities"* (Strom, 2007)

In his article *Social enterprise - the fledgling fourth sector* in Financial Times June 15th 2009, Chip Feiss asks "Is it possible that a whole new, distinct fourth sector is developing right before our eyes? The modern business world has up to now comprised the private for profit, public/ government and non-profit sectors. But today there is a blurring of the lines between these sectors"

It is evident that a new phenomenon is under creation, but at the same time the definitions and descriptions of social entrepreneurship, hybrid organizations and the fourth sector are vague and unclear. As Chip Feiss says, there is a blurring of the lines between the sectors, but neither Feiss nor anyone else really defines how these new lines should be drawn. There is a very obvious need for an operationalization of the sector boundaries.

## 1.2 Research Questions and Purpose of Dissertation

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This dissertation is about the fourth sector and how it came about. It will describe what caused the fourth sector and similar concepts to emerge, what the fourth sector is and what distinguishes it from the other sectors/similar concepts. It will also look into whether fourth sector companies have any competitive advantages/disadvantages and what these could be.

In order to find out what enabled the rise of the fourth sector and how it became relevant, the dissertation will start with an analysis of changes in the global macroenvironment (chapter 2). This is to fully understand the roots of an increase in supply and demand for a reformed

version of capitalism and for new ways of creating both financial and social value in organizations at the same time. Then the dissertation will discuss the emerging popularity of certain concepts of social value creation in the private sector (CSR, CRM, the triple bottom line – chapter 3) and financial value creation in the social sector (social entrepreneurship, social business – chapter 4), and how this leads to a convergence of sectors towards a new intersection of hybrid organizations focused on dual value creation (that some call the fourth sector) in chapter 5.

The fourth sector will be defined (in Chapter 6) through a critique of similar concepts and with a new, more operationalized and applicable definition that will help to clarify what distinguishes the fourth sector from the private sector and the social sector, and what distinguishes fourth sector companies from socially responsible private companies, enterprising nonprofits, social enterprise and social businesses. The dissertation will look at the two axes *private sector vs. fourth sector*, and *social sector vs. fourth sector*, and find out where exactly the dividing lines are. This has not been done for the fourth sector yet – especially not for the axis between the private sector and the fourth sector, formerly categorized as a dichotomy of either 100% private or 0% private (and nothing in between). Through this part it will become clearer where the fourth sector belongs.

The last part of the dissertation will look into if the fourth sector potentially could be a competitive alternative to the private sector. Can fourth sector companies have any competitive advantage/disadvantages due to their greater good-purpose (all other things held equal)?

In order to answer this research question, it is important to isolate the competitive advantages that can arise from the business model of fourth sector companies. The fourth sector business model is assumed to affect the company's relational capital in particular, especially the company's relations with its stakeholders. All other things that can lead to competitive advantages for a company (private or fourth sector) will have to be held equal – assuming that a private sector company and a fourth sector company in theory will perform equally well since they both take use of ordinary market mechanisms and traditional business tools in their everyday operations.

The discussion will be rooted in traditional strategy theory, with resource based theory as a starting point. The strategy theory will be presented in chapter 7 and chapter 8 will present empirical data and conduct a strategic analysis of two fourth sector companies – the Swedish power company God El and the Canadian apparel company Me to We Style. Then the dissertation will be concluded in chapter 9, and some future implications of the phenomenon the fourth sector will be discussed.

## 1.3 Structure

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1. Introduction
2. Changes in the macroenvironment. A prologue that will describe a series of relevant contemporary events in the world the last two decades, leading to changes of the conditions and forces in the wider macroenvironment, societal changes and progress that has enabled the rise of the Fourth Sector
3. A chapter dedicated to trends and concepts related to social value creation in the private sector, such as corporate social responsibility, cause related marketing, and the triple bottom line
4. A chapter looking at relevant trends of financial value creation coming from the social sector, such as social entrepreneurship and social business
5. The two major trends from the chapters above (social value creation in the private sector & financial value creation in the social sector) imply that the sectors are converging towards a new sector. This chapter looks at current descriptions and definitions of this intersection of dual value creation.
6. Criticism of definitions from the three chapters above, leading to a new definition of the Fourth Sector: What it is, what it is not.
7. Competitive Strategy – theory presentation
8. Empirical data and analysis
9. Conclusion and Implications

## Chapter 2 – Setting the stage

*“Our biggest challenge this century is to take an idea that seems abstract—sustainable development—and turn it into a reality for all the world’s peoples.”*

Kofi Annan, former UN Secretary General  
(Hohnen & Potts, 2007)

In just the last two decades, the world has seen enormous progress (and is hungry for more). A series of events has brought us to where we are today – with global opportunities and challenges for new generations and a new millennium. Aggregated, these events have shaped the backdrop for- and enabled the rise of the Fourth Sector.

This chapter will focus on presenting contemporary macro- and micro-changes in society that are an important analysis in order to explain the background for why the world nowadays see more new, experimental solutions to old problems and world issues coming up than ever before. The analysis presented in this chapter shows changes in the conditions and forces in the wider **macroenvironment**, defined as *“the broader economic, technological, demographical, social and political context in which companies and industries (and sectors) are embedded”* (Hill & Jones, 2004).

The chapter will be structured in two main parts, called “Macro-changes in Society” and “Micro-changes in Society” - with respective sub-categories, illustrated in Figure 1 below:

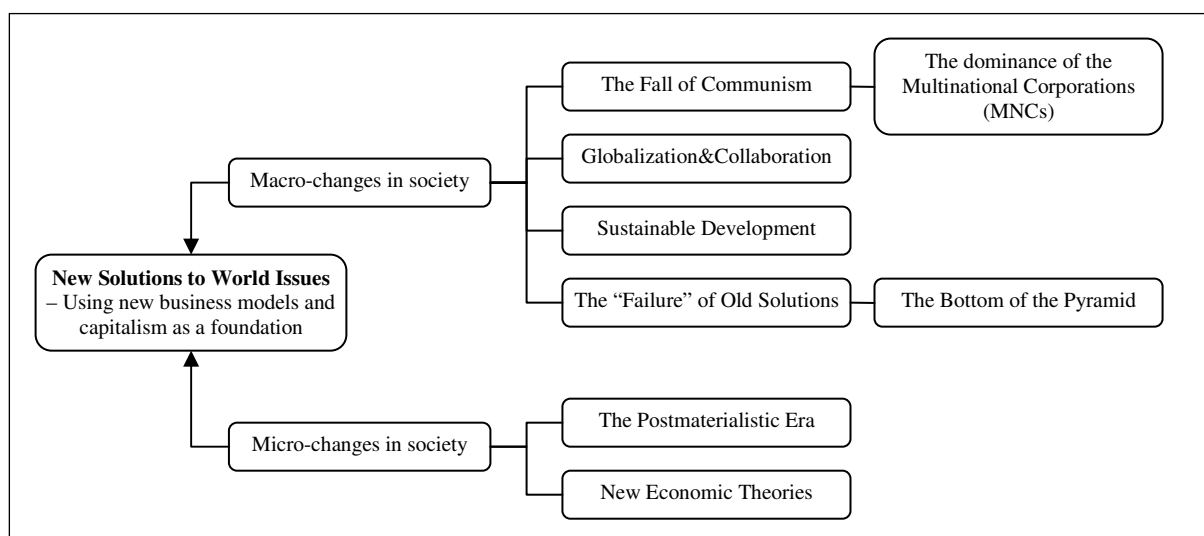


Figure 1 - A visualization of Chapter 2

# Macro-changes in Society

These societal changes are relevant background for understanding why capitalism today is both praised and under fire at the same time, and why supply and demand for using capitalism in a different, more humanistic way is increasing. Recognizing the reasons for this increased supply and demand (for an improved version of capitalism) is essential for understanding the emergence of a new sector of hybrid organizations creating social and financial value at the same time.

## 2.1 The fall of communism

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November 9<sup>th</sup> 2009 marks the 20 year anniversary since the fall of the Berlin Wall - an event that opened up the world in unexpected ways. Communism was abandoned and left as nothing more than an ideological, impractical Utopia, whereas Capitalism came out as the winner – gradually opening up and changing political systems all over the world towards individual rights, free markets, open economies and private ownership.

These changes really began after the end of World War II in 1945, when a lot of work was done to reconstruct and restore the economic system and international trade in the so-called first world (Europe, United States, Canada, Japan). Currencies became convertible again; trade barriers came down with the GATT agreement of 1947 (and also later rounds of negotiations), and an effective market-based trading system lead to rapid economic growth (Sachs, 2005, p. 47). But with the end of World War II, political divisions in the world were stronger than ever and had obvious negative implications for world trade and market cooperation. The second world<sup>1</sup>, the socialist world, remained economically and politically separate from the first world until the fall of the Berlin Wall in 1989 and the fall of the Soviet Union in 1991:

“The fall of the Berlin Wall unleashed forces that ultimately liberated all the captive peoples of the Soviet Empire. But it actually did so much more. It tipped the balance of power across

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<sup>1</sup> ”The overriding characteristics of the second world were state ownership of the means of production, central planning of production, one-party rule by communist parties, and economic integration within the socialist world combined with economic separation from the first world” (Sachs, p.47)

the world toward those advocating democratic, consensual, free-market-oriented governance, and away from those advocating authoritarian rule with centrally planned economies. The Cold War had been a struggle between two economic systems – capitalism and communism – and with the fall of the wall, there was only one system left and everyone had to orient himself or herself to it one way or another” (Friedman, 2007, p. 57).

There was also the third world – post-colonial countries emerging from imperial domination, countries that wanted to develop on their own, choosing not to be a part of the capitalist first world nor the socialist second world (Sachs, 2005). Both the second world and the third world closed themselves off from global economic progress and the advance of technology until the early 1990s, when they realized that their old political and economical systems did not work (countries loaded with debt, inflation, economic instability and lagging behind on technology) and several of these countries again wanted to be a part of the global economy (ibid).

The fall of communism implied that the strength and scope of capitalism as a system was drastically expanded, and this brought economic growth and affluence to millions of people. Supply and demand for capitalistic solutions increased, but the old system was at the same time left behind (the former communist/socialist system), a system that in theory was meant to directly benefit the public good (where capitalism benefits the public good indirectly through a free-market system).

## 2.2 The dominance of the MNC

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Since the fall of communism the new global dynamics shifted in favour of the large multi-national companies (MNCs)<sup>2</sup>, companies utilizing the new open economies and the shift to capitalism in numerous new countries across the globe. Foreign direct investment (FDI) by multi-national companies overtook official development assistance (ODA) in the 1990s, and by year 2000, FDI exceeded ODA by more than a factor of 5. There are now more than 60,000 MNCs with more than a quarter million affiliates around the world, accounting for more than 25 percent of world economic output but employing less than 1 percent of the world’s labour force (Hart, 2005).

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<sup>2</sup> MNCs are defined as any corporation with operations in more than one country (Hart, 2005)

At the same time, there has been substantial criticism towards the MNCs and their global dominance; given the 10 largest MNCs have annual sales of more than the GNPs of the 100 poorest countries in the world. Wal-Mart's revenue in 2008 alone was \$378,799,000,000 (Yahoo Finance, 2009) making them the world's 33<sup>rd</sup> biggest economy. This is more than the 2008 GDP for countries like Sweden, Austria and Switzerland and oil economies like Venezuela, U.A.E and Nigeria (CIA World Factbook, 2009).

Statistics like this obviously raises concerns about the shift of power towards MNCs and the decrease in sovereignty and influence of governments around the world, especially given the lack of regulations in the private sector and the worldwide commercialization of culture based upon western values promoted by the MNCs. In addition, there are hundreds of stories from the last two decades of exploitation of people and the planet by the MNCs (the use of child and sweatshop labour, the destruction and ruthless exploitation of the environment) as a consequence of the chase for higher profits at the expense of moral standards. This has led to worldwide boycotts of- and protests against these companies, and the debate on Corporate Social Responsibility and Corporate Citizenship has gained momentum parallel to the growth and increased influence of the MNC. The World has also seen defining events in the new millennium such as the fall of Enron and other corruption scandals on Wall Street in 2001-2002, and the Financial Meltdown and World Recession in Q4 2008 and Q1 2009, leading to multiple heated discussions on corporate transparency, corporate governance and greed – with worldwide governmental stimulus packages and bailout plans, new suggestions for market rules and regulations, and even discussions on the purpose and organization of capitalism as a system has been consequences of these events.

With the increased power of the MNC, there is also an increased demand that powerful companies in the private sector behave socially responsibly as the global citizens they are. This increased demand leads to a trend of more social value creation in the private sector.



## 2.3 An era of globalization and collaboration

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A major contribution to contemporary globalization was obviously the fall of the Berlin wall and the fall of the Soviet Union. The world was opened up and capitalism was introduced to a range of new countries – making cooperation easier across borders that previously had been closed. And with capitalism came an even stronger focus on private rights, and the values of freedom and individualism.

But there is yet another revolution that has shaped the current era of globalization more than anything else and made globalization turbocharged, namely the Information Revolution. In just a few years in the early 1990s, a series of information technology innovations were commercialized and made available for the global mass markets: the PC got an user-friendly interface in Windows 3.0 and became available to the public at an affordable price point, the Internet emerged as a cheap, convenient global tool for connecting people, cell-phones crossed the market chasm and became an essential part of daily communication between human beings around the world, and in 1991 Tim Berners-Lee created the World Wide Web and posted the world's first website while working for CERN in Switzerland.

The Information Revolution has since the early 1990s radically altered the way we live our lives and communicate, at an accelerating pace. The number of internet hosts has grown exponentially since 1992 (Internet Systems Consortium) and the number of internet users and new websites are growing in the millions every year. Back in 1965, Intel co-founder Gordon Moore predicted that the number of transistors on a chip will double about every two years – a prophecy that has proved it's right to existence ever since, under the name Moore's law ([www.intel.com/technology/mooreslaw/index.htm](http://www.intel.com/technology/mooreslaw/index.htm)).

With technological progress, the world is growing smaller and smaller, bringing people closer together than never before. Travel costs has been lowered, the World Wide Web is at our fingertips, we have social networking as a second life (you choose where to live and be your best), 24/7 online collaboration, real-time continuous streams of news and personal stories, and constant updates on what's happening all over the globe. Everyone with a cell-phone camera and access to the internet can become a star-reporter with millions of readers and viewers – which also means it's more difficult to hide away from the public light for the rest

of us. The world is inevitably getting more transparent, and there is nothing we can do about it. This is the era of collaboration and decentralization, empowering individuals all over the world. As Warren Bennis puts it: *“None of us is as smart as all of us.”* (Bennis, 1998). One can now start and run a born-global business from anywhere in the world, just through access to the internet and with very basic web-skills. The implications of the Information Revolution are enormous new opportunities for hundreds of millions of people in developing countries that previously have been kept out of the economic growth and prosperity that the capitalistic system can provide. The supply of new creative solutions and new approaches to capitalism has increased drastically through the IT-revolution.

## 2.5 Sustainable Development

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*“To meet the needs of the present without compromising the ability of future generations to meet their own needs”*

The Brundland Commission’s definition of Sustainability, Our Common Future, 1987

Sustainable Development and Sustainability are words used with increased frequency the last five years; in everything from media, to speeches, corporate strategies, public policy making and in bold NGO vision statements. Global Warming has been on the global agenda for roughly two decades now, and the Kyoto agreement of 1997 is supposed to be replaced with a new and better agreement from a meeting in Copenhagen in December 2009. The expectations to the meeting are enormous; the World might get its first truly global agreement on reducing carbon emissions and the effect of global warming. With the United States of America and President Barack Obama in the forefront for sustainable development, Copenhagen 2009 might be one of the defining events of this century, some even say of contemporary human history. Even the Economist names this event as one of the most important events of this year in their editorial in “The World in 2009”, and even chose to publish a special section on the environment to underline the importance of this issue.

The Green Movement has seen enormous progress (and hype) the last 5 years, after the Nobel Committee awarded the Peace Prize to both Dr. Wangari Maathai, and Albert Arnold Gore Jr. and the Intergovernmental Panel on Climate Change) in 2004 and 2007 respectively, establishing the fight against global warming as an important and relevant process to secure

world peace. That Al Gore's speech "An Inconvenient Truth" was made into a documentary which won the Oscar Academy Award in 2007 didn't exactly tone down the Green Movement either. Currently, the entire world is discussing energy efficiency and new green collar jobs, and President Barack Obama has energy and the environment on the top of his list of priorities, alongside with the economy and global security.

The current version of the green movement dates back to 1983, when the United Nations convened the World Commission on Environment and Development, also known as the Brundtland Commission (after its Chair Gro Harlem Brundtland), to address growing concern "about the accelerating deterioration of the human environment and natural resources and the consequences of that deterioration for economic and social development." In establishing the commission, the UN General Assembly recognized that environmental problems were global in nature and determined that it was in the common interest of all nations to establish policies for sustainable development (Brundtland Commission, 1987). The Report of the Brundtland Commission, "Our Common Future", was published by Oxford University Press in 1987, with the following definition of sustainable development, word for word extracted from the report:

1. Sustainable development is development that meets the needs of the present without compromising the ability of future generations to meet their own needs. It contains within it two key concepts:

- the concept of 'needs', in particular the essential needs of the world's poor, to which overriding priority should be given; and
- the idea of limitations imposed by the state of technology and social organization on the environment's ability to meet present and future needs.

2. Thus the goals of economic and social development must be defined in terms of sustainability in all countries - developed or developing, market-oriented or centrally planned. Interpretations will vary, but must share certain general features and must flow from a consensus on the basic concept of sustainable development and on a broad strategic framework for achieving it.

3. Development involves a progressive transformation of economy and society. A development path that is sustainable in a physical sense could theoretically be pursued even

in a rigid social and political setting. But physical sustainability cannot be secured unless development policies pay attention to such considerations as changes in access to resources and in the distribution of costs and benefits. Even the narrow notion of physical sustainability implies a concern for social equity between generations, a concern that must logically be extended to equity within each generation.

4. The satisfaction of human needs and aspirations in the major objective of development. The essential needs of vast numbers of people in countries of the global South for food, clothing, shelter, jobs - are not being met, and beyond their basic needs these people have legitimate aspirations for an improved quality of life. A world in which poverty and inequity are endemic will always be prone to ecological and other crises. Sustainable development requires meeting the basic needs of all and extending to all the opportunity to satisfy their aspirations for a better life.”

Even though the Brundtland Commission was originally convened to look at environmental and natural resource challenges, the impact of the commission has turned out to be substantially wider, both being a driving force for environmental compliance and strategies, but also towards more social issues and sound economic development as well. Wikipedia coins the term rather precisely: *“Since the 1980s, the idea of human sustainability has become increasingly associated with the integration of economic, social and environmental spheres”* (Wikipedia).

In other words, sustainability as a concept has also turned out to be increasingly important in the creation of balanced strategies for the private, public and nonprofit sectors, with the Green Movement as an important sub-category. Both supply and demand for new ways of doing business in a more sustainable way has increased because of this concept.

## 2.6 The “failure” of old solutions

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Even though some of the emerging economies of the world (like China and India) are bringing millions of people out of poverty every year through their countries’ participation in the capitalistic system, large parts of the world are still struggling with basic issues like health, poverty, education and hunger.

In his book *The White Man's Burden* (2006), William Easterly brutally confronts the fact that the West has spent \$2.3 trillion on **foreign aid** the last five decades without really solving any major problems for the world's poor and needy people. He goes as far as calling this a second tragedy for the world's poor, claiming that the reason for the tragedy is the mistaken approach that traditional Western assistance takes toward world poverty.

At this point in history, human beings in theory have the financial capacity to eradicate extreme poverty and hunger, and solve most of the world's latent issues if resources were redistributed in a more efficient way. This was also addressed at the start of this millennium by the United Nations, where political leaders around the world agreed on the Millennium Development Goals – goals that was promised to be met by 2015 <sup>3</sup>. Now, more than half way into the programme, the UN admits that many of the goals will not be met in time (United Nations, 2008)

On a global scale, [extreme] poverty is far away from being eradicated and other important issues are not even close to being resolved, even though national governments, the World Bank, the International Monetary Fund, aid agencies and civil society has been trying hard to fight these issues the last 50 years. More than 4 billion people live on less than 2 dollars per day (adjusted for purchasing power), and global differences has only increased (Prahallad, 2006). This is also emphasised by William Easterly (2006, p. 8) "Eight hundred and forty million people in the world don't have enough to eat. Ten million children die every year from easily preventable diseases. AIDS is killing three million people a year and is still spreading. One billion people in the world lack access to clean water, two billion lack access to sanitation. One billion adults are illiterate. About a quarter of the children in the poor countries do not finish primary school." Easterly argues that the UN development goals and other compassionate dreams of change voiced by visionaries, celebrities, presidents, and bureaucracies are mostly unrealistic dreams that no-one is really accountable for, and that the world needs less fluffy promises like this (from so-called "planners"), and more practical, local solutions that actually works (from so-called "searchers"). In Easterly's opinion, a planner "thinks of poverty and other issues as a technical engineering problem that his

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<sup>3</sup> The eight Millennium Development Goals are (1) eradicate extreme poverty and hunger, (2) achieve universal primary-school enrollment, (3) promote gender equality and empower women, (4) reduce child mortality, (5) improve maternal health, (6) combat HIV/AIDS, malaria, and other diseases, (7) ensure environmental sustainability, and (8) develop a global partnership for development (Easterly, 2006, p.9)

answers will solve, that outsiders know enough to impose solutions”, but a searcher “admits he doesn’t know the answers in advance, he believes that poverty is a complicated tangle of political, social, historical, institutional, and technological factors, and hopes to find answers to individual problems only by trial and error experimentation, that solutions must be homegrown” (Easterly, 2006, p. 6)

According to Stuart Hart in his book “Capitalism at a crossroads” (Hart, 2005, p. xxv) the gap between the richest and the poorest in the world has widened the last 40 years. In 1960, the richest 20 percent in the World accounted for 70.2 percent of global GDP, increasing to 85 percent in year 2000. The poorest 20 percent controlled 2.3 percent of global GDP in 1960, decreasing to only 1.1 percent in 2000. The rich to poor GDP ratio has therefore increased from 30:1 in 1960 to 80:1. The global economic pyramid (shown in Figure 2 below) clearly shows the imbalance of purchasing power in the world.

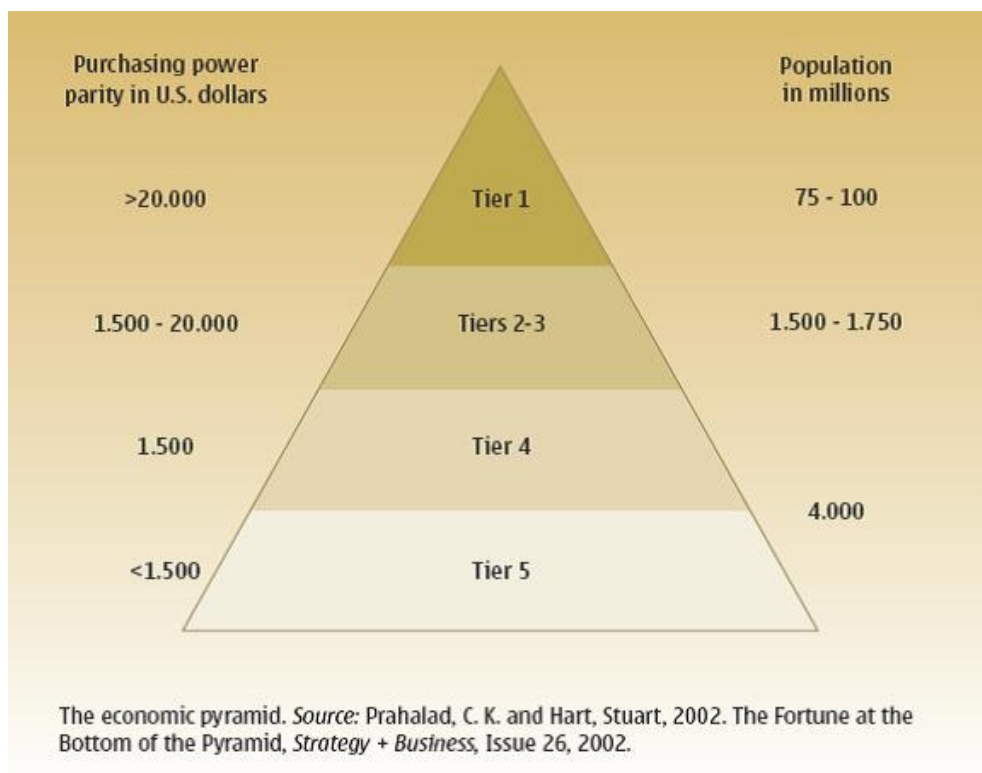


Figure 2 - The Economic Pyramid

### 2.6.1 The Bottom of the Pyramid

In his book, *The fortune at the bottom of the pyramid (BOP)*, C.K. Prahalad (2006, p. 1) proposes that “we stop thinking of the poor people in the world as victims or as a burden, and start recognizing them as resilient and creative entrepreneurs and value-conscious consumers”.

Prahalad suggests a framework for poverty alleviation, where he challenges private companies, government, development agencies and the poor themselves to start working together with a shared agenda – where entrepreneurship and business is the key to social change and economic development. This interconnectedness and cooperation between the different stakeholders / sectors are visualized in the following model/framework (Figure 3):

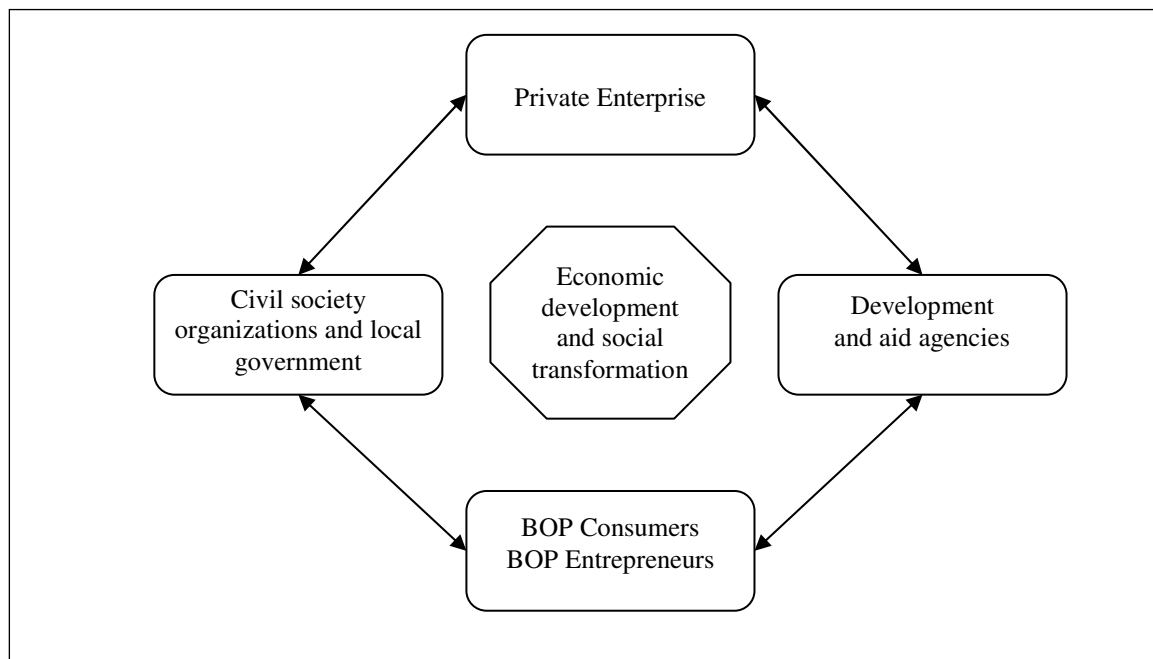


Figure 3 - The fortune at the bottom of the pyramid (Prahalad, 2006)

Prahalad suggests that markets should be built for the people at bottom of the pyramid. This approach asks for a partnership with the poor in order to innovate and achieve sustainable win-win situations, where both the poor are engaged and the companies providing them products or services are profitable. This is certainly not another Corporate Social Responsibility-initiative, but a part of a company’s core business offering. Prahalad (2006) argues that “there is significant untapped opportunity for value creation (for BOP consumers, shareholders, and employees) that is latent in the BOP market, markets that have remained “invisible” for too long”

# Micro-changes in society

## 2.7 The Postmaterialistic Era

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After World War II, the first world has experienced an undeniable material success through capitalism and successful political interventions. In general, living standards in developed countries are high and extreme poverty is not really an issue anymore. Self-expression becomes more important, and quality of life, environmental protection, social justice, diversity, equality, personal freedom and individualism is in focus.

With increased living standards, unprecedented affluence, greatly increased educational levels, expanding information opportunities and an extensive social welfare system follows an interesting change in the public's basic value priorities – trends that are altering socioeconomic conditions and changing the relative scarcity of valued objects of these nations (Dalton, 2002, p. 80)

Ronald Inglehart has systematically tried to describe the value changes that are transforming advanced industrial societies, and bases his theory of value change on two premises (Inglehart 1981, in Dalton p.80):

- i) Basic value priorities are determined by a scarcity hypothesis. Individuals place the greatest value on those things that are in relatively short supply. This hypothesis is formed with basis in Abraham Maslow's theory on hierarchy of needs from 1954, where people are first driven to fulfil basic and safety needs, before continuing the search for higher-order needs such as belonging and self-esteem, participation and then self-actualization through the fulfilment of aesthetic and intellectual potential
- ii) One's value priorities reflect the political and economical conditions that prevailed during one's preadult years (socialization hypothesis).

These two hypotheses leads to a model of value change in society, and Inglehart has drawn parallels between Maslow's basic needs and *material* values and goals, and between higher-order needs and *postmaterial* values. In other words, after people reach a satisfactory level of



material safety, they will start focusing more on postmaterial values such as self-actualization.

According to Dalton's revision of several surveys in *Citizen Politics* (2002), postmaterialists are most common in nations with high living standards (and less prevalent in less affluent nations). He claims that "the greatest shift in values occurs during the transition from a subsistence economy to an advanced industrial society, such as that found in postwar Western Europe. Once this level of affluence is achieved, further increases in well-being produce progressively smaller changes in values, e.g. that the process of value change will continue at a slower, but continuing, rate in the future.." (Dalton, 2002, p. 86)

In addition, younger generations have stronger postmaterialistic values than older generations (in accordance with Inglehart's socialization hypothesis). With a constant growth in educational levels and economic and social affluence in developed countries around the world, later generations are more postmaterialistic than ever (ibid). This can be observed with the current Generation Y (The Millennials), people in developed countries born between 1978 and 2000 – a "spoiled" generation of young people that has grown up under safe, materialistic circumstances, hence this generation's urge to move beyond pure economic needs and go down the path of self-actualization, caring more about helping others and going good in the world than any generation before them. Because of their different set of values, this generation (and later, even more postmaterialistic generations) will shape the world in new, unpredictable ways. These findings are undeniably good news for a world facing important challenges and unsolved issues. It is fair to assume that with these new generations, there has been (and will continue to be) an increased supply of and demand for postmaterialistic structural/systemic solutions (organizations, companies, careers etc) in the developed world.

## 2.8 New economic theories of human motivation

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In the last couple of decades, the field of conventional economics has been completely revamped by opening up to interdisciplinary ideas of human motivation and behaviour from psychology, biology and sociology.

Traditional economic theory explains that people will always act in ways that maximizes their personal utility (interpreted as personal material wealth), under the assumptions of rational choice models: human beings are always guided by narrow economic self-interest and the ability to make rational decisions:

*“The concept of man currently used in economics assumes that individuals maximize their own utility subjects to the constraints imposed most importantly by income and time. He or she is taken to be egoistic and to be interested mainly – and sometimes wholly – in material values only (wealth maximization hypothesis). This is the crude model of Homo Oeconomicus which has proved able to explain a surprisingly large share of human behaviour”* (Frey, 1997, p. 118).

The most central and universally valid prediction of the traditional Homo Oeconomicus is the Price Effect, where a higher monetary reward (price) induces more of an activity (Frey p.119).

But are human beings really acting with such a narrow self-interest in real life? Many human actions seem to be at odds with this assumption. People don’t act just because they expect a monetary gain, people don’t work just because they get paid. And if people always acted with narrow self-interest as the only motivation, why would you donate money to charity, return a strangers lost wallet, give blood and leave tips at restaurants that we will never visit again? (Frank, 2004).

Several contemporary economists have been questioning the behavioural simplicity of the Homo Oeconomicus, arguing that this model is ready to be replaced with an economic theory of human motivation not restricted to monetary incentives, but where moral motivation, social motivation and intrinsic motivation also should be taken into consideration, since these are common traits of most human beings<sup>4</sup>.

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<sup>4</sup> In his collection of essays, *What Price The Moral High Ground* (2004) Robert H. Frank even shows that people’s likelihood of making selfish choices in social dilemmas rise sharply with their exposure to training in economics.

The emergence of so-called pro-social behaviour is gradually being documented through a variety of arguments, experiments and other empirical evidence, some of them presented in Robert Frank's collection of essays "*What price the moral high ground*" (2004), in Bruno Frey's "*Not just for the money*" (1997) and in numerous articles by Ernst Fehr, Armin Falk, Alexander Cappelen, Bertil Tungodden and Gaute Torsvik.

In *Not just For the Money*, Bruno Frey introduces a modified, more psychological model of human behaviour: The Homo Oeconomicus Maturus, where the traditional Homo Oeconomicus is replaced with a more "mature" man with a more refined motivational structure, accounting for that:

- i) intrinsic motivation can be an important determinant for human behaviour,
- ii) monetary incentives (under identifiable conditions) can undermine intrinsic motivation (called the Crowding-Out Effect)
- iii) other external interventions may also produce a Crowding-Out Effect (in addition to monetary incentives, such as commands and punishment)
- iv) intrinsic motivation can be bolstered with external interventions under certain conditions

In other words, opposite to the prediction of the Price Effect, monetary rewards doesn't necessarily lead to increased activity, but can actually "crowd-out" intrinsic motivation attached to a specific work task (mowing your grandparents lawn can be a rewarding task in itself, knowing that you are doing a good deed. You don't need payment for the job, and getting paid could actually reduce your motivation for doing this in the future).

Frey also presents several other behavioural anomalies that are inconsistent with the model of man used in traditional economic theory, and argues that the axioms of rationality are systematically violated and the "commonly used utility maximization model is no longer appropriate" (Frey, 1997, p. 120) Ernst Fehr and Armin Falk argues for a similar model in their article "Psychological foundations of incentives" (2002), showing that "monetary incentives may backfire and reduce the performance of agents or their compliance with rules", and that "reciprocity, social approval, social norms and task-specific motives may generate very powerful incentives themselves" (Fehr & Falk, 2002, p. Abstract). This has got important implications for human behaviour and performance.

In several lectures (SAM464, Norwegian School of Economics, 2006) Alexander Cappelen summarizes all of these theories into three categories of human motivation that interacts with economic incentives and influences human behaviour:

- i) Moral Motivation (altruism, reciprocity, fairness)
- ii) Social Motivation (social approval, social norms)
- iii) Intrinsic Motivation (task-specific motivation)

For all these forms of human motivation, there are several optional utility functions, depending on the situation and the individual's personality and preferences, changing the traditional field of utility maximization completely into something more complex, mature, and with a much closer resemblance to real life situations (Cappelen, 2006). Human behaviour consequential to moral, social or intrinsic motivation could still be in accordance with self-interest, but not in the narrow, materialistic sense self-interest has previously been interpreted. Many human beings are pleased by the happiness of others, and by being able to contribute to the happiness of others, something that can explain anonymous philanthropy, charitable giving and volunteering. It can therefore be claimed that altruistic behaviour can be egoistic and in one's self interest in the pursuit of happiness:

*"How selfish soever man may be supposed, there are evidently some principles in his nature, which interest him in the fortunes of others, and render their happiness necessary to him, though he derives nothing from it, except the pleasure of seeing it".*

- Adam Smith, Theory of Moral Sentiments (Cappelen, Lecture 2006)

Aggregated, the new models of human motivation and behaviour make it clear that the old, straightforward Homo Oeconomicus needs to be replaced (but not forgotten, since elements from Homo Oeconomicus always will be valid) with the new, better and more complex Homo Oeconomicus Maturus – defined in an even wider sense than that of Bruno Frey in "Not just for the money" (1997).

There are several implications of this in real life, such as:

- New solutions to the classical principal-agent problem on a personal, organizational and structural (political) level, such as compensation and incentives, contracts, public policy and environmental policy.
- Pricing of goods and services
- Public Regulations, Tax and Welfare policies
- Official Development Assistance, International Development and poverty fighting
- Corporate strategies and the pursuit of profit maximization: Can profits increase through a more complex stakeholder-approach, taking different forms of stakeholder motivation into consideration? Should profit maximization be the only goal, given the more complex model of human utility maximization?

## 2.9 Chapter Analysis

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The ambition of this chapter has been to explain the backdrop for the creation of the Fourth Sector, for increased corporate social responsibility in the private sector and the rise of new business models and creative solutions in the nonprofit sector. These initiatives and solutions might help to solve classical global issues such as extreme poverty and hunger, but also local issues not satisfactorily addressed by local government, the private sector or non-governmental agencies.

The new organizational structures, strategies and business models arise as a consequence of a series of coinciding events. The fall of the Berlin Wall in 1989 and the fall of the Soviet Union in 1991 opened up an entire socialistic world to the capitalistic system, increasing the size of the world marketplace drastically and incorporating hundreds of millions of people to take part in new economic growth and affluence. The power and influence of big, multinational companies (MNCs) increased as a consequence of easier access to markets, and several MNCs exploited their increased power in the 1990s to grow their profits on the expense of poor people and the planet. The public response was a range of anti-MNC and anti-globalization protests, over time forcing large MNCs to gradually realize their role as global citizens and the social responsibility that comes with the increase of global power and influence. Other events in the financial sector, such as the fall of Enron and the economic meltdown in 2008-2009 has also led to a demand for a more responsible private sector, with

less greed and more transparency and social responsibility. In the current economy (Q1-2009), survival is the main objective, but is combined with the demand for social responsibility and sustainable development in a fascinating way.

At the same time, the world has seen an information technology revolution since the start of the 1990s setting the stage for a turbocharged version of globalization, making the world a lot smaller and more tightly knit together. The age of the PC, the Internet and the World Wide Web has launched a new era of collaboration and community, and even though this is all intangible – around everywhere and right next to you - it creates amazing (low-cost) opportunities for people all over the world. The people of the world are now more connected than any time before in history, something that makes it easier to see where the real needs and demands are, get feedback from people all over the place, and collaborate with your stakeholders on new projects. New business models arise based on the new tools available, such as Kiva.org – a social network that tells stories of poor people all around the world that needs microloans and connects them with richer people that can provide them with the microloans they need to grow their small (and big) local businesses. The payback rate for the loans is 98.75%, so this cannot be classified as charity. Its business, but a new kind of business that exists to do good and help people that needs it.

Another concept that has largely influenced this world the last two decades is the idea of *sustainability*. This is most often interpreted with the environment in mind, and the intensity of discussions around global warming, carbon emissions and a greener planet has only increased since the late 1980s, with an extra hype after 2004 and 2007 with two Nobel Peace Prizes related to environmental work. Governments and companies have realized that there are money to be made from going green and making societies more energy efficient, regulations and laws are being passed, eco-friendly products are selling like never before and thousands of new environmentally-friendly companies are being founded.

But in the original idea developed by the Brundtland Commission, the environment was only one (important) part of the concept sustainability. Sustainable economic and social development was equally as important, and this focus has inspired thinkers all over the world to develop so-called triple bottom line thinking, strategies and reporting. The triple bottom-line is valid for all sectors in society, and in this field sustainable economic, environmental

and social development goes hand in hand. The idea of the triple bottom-line will be addressed more thoroughly in the next chapter.

Even with increased focus on the triple bottom-line, several contemporary economists such as William Easterly, C.K.Prahalad and Stuart Hart are unhappy with how slow the progress has been in this world when it comes to solving important world issues through ODA. Easterly, Prahalad and Hart claim that the differences between rich and poor are getting bigger and that leaders of world should have been able to solve more problems the last fifty years that they actually have. They all speak up for new solutions to get people out of extreme poverty and hunger, where traditional official development assistance (ODA) has got a less important role. Easterly, Prahalad and Hart all feel that solutions should be developed locally where the need is, in a more bottom-up approach than before. They all speak warmly of capitalism and business as the core system to achieve social change, and C.K. Prahalad (2006) even suggest a framework for poverty alleviation, where the “*Bottom of the Pyramid*” (the world’s 4 billion poor) can work together with private companies, aid agencies, local governments and civil society to find smart, creative, market-based entrepreneurial solutions that can help address some of their needs. Muhammad Yunus’ microfinance-institution Grameen Bank in Bangladesh is mentioned as one such successful example.

On a micro-level, there have also been remarkable changes the last two decades. Based on social studies by Ronald Inglehart and Russell J.Dalton, it might look like good old Abraham Maslow had a point with his hierarchy of human needs. Inglehart and Dalton shows that Western countries have entered a post-materialistic era, where self-actualization, helping others and a less materialistic-focus are more relevant than ever before, and that this is actually increasing with new generations. If this is viewed in combination with new economic theories of human motivation from the last two decades, the results are quite remarkable. Several modern economic theories are stating that the old version of the economic man is ready to be replaced with a new Homo Oeconomicus Maturus – the mature economic man, a model that has a much closer resemblance to the way human beings act and interact in the real life. This shows that our rationality, self-interest and utility is highly affected by other motivations than just financial reward; that moral, social and intrinsic motives such as the desire to do good, the desire to reciprocate, what is fair (and the varying human interpretation of fairness), what others think and do, what is “normal” in society, and the value of the work-task and action in itself.

Combined, the theories of postmaterialism and the theories of the mature economic man can be interpreted towards that human behaviour, motivation and performance is more complex than ever, but that moral and society also is more relevant (in an academic perspective) to human beings than ever before. When that is said, the father of Capitalism Adam Smith also touched upon this in *The Theory of Moral Sentiments* – before he wrote *The Wealth of Nations*.

Summarized, overarching changes in society (changes in technology, the social environment, the economy, demography and political forces) have led the world to where it is today – a world where there is both a supply and demand for social and moral change. There is enlightened self-interest amongst human beings and the ability and willingness to change the world through new organizational structures and business models is greater than ever before. This explains the backdrop for the rise of an entire new sector of hybrid companies focused on creating both social and financial value.



## Chapter 3 – Trends and concepts related to social value creation in the private sector

There are two direct consequences of the macro- and micro-changes in society presented in chapter 2 that will be relevant for the next two chapters:

- i) Increased focus on social value creation in the private sector
- ii) Increased focus on financial efficiency in the social sector

This chapter will define some of the most important trends and concepts relevant for social value creation in the private sector. The concepts that will be focused on are Corporate Social Responsibility (with sub-fields such as corporate citizenship, corporate philanthropy and corporate social initiatives), Cause Related Marketing and the Triple Bottom Line. The popular concept “sustainability” has already been defined in chapter 2, but is also relevant for this chapter since it is a commonly used phrase in companies around the world. .

Where this chapter (chapter 3) will look at trends of social value creation in the private sector, the next chapter (chapter 4) will describe two important trends that blends financial value creation into the social sector, namely *social entrepreneurship* and *social business*. Chapter 5 will claim that the trends described in chapter 3 and 4 leads to a convergence of the sectors, creating hybrid organizations of dual financial and social value creation that constitutes a new, emerging fourth sector. Chapter 6 will provide a new definition of the fourth sector.

The table below shows briefly the popularity of some of the concepts mentioned above:

Number of hits in Google (June 2009)			
“corporate social responsibility”	3,450,000	“business ethics”	3,590,000
“corporate citizenship”	1,940,000	“green business”	5,140,000
“corporate philanthropy”	259,000	“social investment”	598,000
“sustainability”	32,600,000	“cause related marketing”	198,000
“corporate sustainability”	258,000	“social enterprise”	2,190,000
“sustainable business”	1,230,000	“social business”	581,000
“triple bottom line”	371,000	“fourth sector”	29,500

Table 1 - Number of hits in Google

### 3.1 Corporate Social Responsibility

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What is the purpose of a business? Who is it for, why does it exist, and how should it conduct its daily operations?

These are essential questions all business owners and business leaders ask themselves at all times, and the answers are ambiguous. As all human beings are unique, so are also organizations and businesses - because they are founded by individuals with different ideas in mind of what they want their organization to achieve. The main motive of private sector businesses has always been, and will probably always be to maximize profits. This is in the nature of the private sector itself.

As chapter 2 described, there are more multinational companies now than ever before, and their foreign direct investments were in year 2000 five times higher than what governments spend on official development assistance (Hart, 2005). The MNCs have got more power than ever, but with more power follows more pressure and tougher demands from government, NGOs, customers and media. And with the information revolution, increased transparency and easier access to information, the public is also very aware of the actions of private sector companies. It is more difficult than ever before to hide unlawful or morally grey actions, and monitoring organizations such as the Fair Trade Labelling Organisation (FLO), the Global Reporting Initiative (GRI), Social Accountability International (SA), and Veritas are all working actively to limit the unethical behaviour of private companies.

There is no doubt that businesses in the private sector are under pressure from different stakeholders to behave in a socially responsible way – but what socially responsible behavior really entails has been thoroughly discussed for many years. Given the nature of this discussion, there is no one universally accepted definition of corporate social responsibility (CSR). David Vogel defines CSR as “*Practices that improve the workplace and benefit society in ways that go above and beyond what companies are legally required to do*” (Vogel, 2005, p. 2). A variety of other definitions are presented in Table 2 on the next page.

DEFINITIONS OF CORPORATE SOCIAL RESPONSIBILITY (CSR)	
Kotler and Lee (2005,p.3)	“Corporate social responsibility is a commitment to improve community well-being through discretionary business practices and contributions of corporate resources.”
(Harvard Kennedy School of Government)	“We define corporate social responsibility strategically. CSR encompasses not only what companies do with their profits, but also how they make them. It goes beyond philanthropy and compliance and addresses how companies manage their economic, social, and environmental impacts, as well as their relationships in all key spheres of influence: the workplace, the marketplace, the supply chain, the community, and the public policy realm.”
(Business for Social Responsibility)	“Operating a business in a manner that meets or exceeds the ethical, legal, commercial, and public expectations that society has of business”
Wikipedia	“CSR is a concept whereby <a href="#">organizations</a> consider the interests of <a href="#">society</a> by taking responsibility for the impact of their activities on <a href="#">customers</a> , suppliers, employees, shareholders, communities and other <a href="#">stakeholders</a> , as well as the <a href="#">environment</a> . This <a href="#">obligation</a> is seen to extend beyond the statutory obligation to comply with <a href="#">legislation</a> and sees organizations voluntarily taking further steps to improve the quality of life for employees and their families as well as for the local community and society at large.”
(Hohnen & Potts, 2007)	“CSR should be seen as the way that firms—working with those most affected by their decisions (often called “stakeholders”)—can develop innovative and economically viable products, processes and services within core business processes, resulting in improved environmental protection and social conditions.”
Working definition, ISO 26000 Working Group on Social Responsibility, Sydney, February 2007 (Hohnen & Potts, 2007)	“Social responsibility (is the) responsibility of an organisation for the impacts of its decisions and activities on society and the environment through transparent and ethical behaviour that is consistent with sustainable development and the welfare of society; takes into account the expectations of stakeholders; is in compliance with applicable law and consistent with international norms of behaviour; and is integrated throughout the organisation.”
Angelidis and Ibrahim (1993) in Brønn 2001	“Corporate social actions whose purpose is to satisfy social needs”

Table 2 - Definitions of Corporate Social Responsibility (CSR)

### 3.1.1 The Shareholder Perspective – Milton Friedman’s view on CSR

One of the defining moments in the CSR-debate came with Milton Friedman’s world-famous article “The Social Responsibility of Business” in New York Times Magazine on September 13<sup>th</sup>, 1970, where Friedman clearly and crisply expresses his views on the subject.

In Friedman’s opinion “there is one and only one social responsibility of business – to use its resources and engage in activities designed to increase its profits so long as it stays within the rules of the game, which is to say, engages in open and free competition without deception or fraud” (Kinsley et.al, 2008, p.297). Friedman argues that a business cannot even have responsibilities, only people can. A corporation is in best case an artificial person, and might therefore have artificial responsibilities. Though, according to Friedman, the corporate executive is an employee of- and agent for the owners of the business and has a direct responsibility to these employers. This responsibility is first and foremost to execute and direct the business in the way the owners desire; most likely to maximize the profits while making sure the business and its employees act in accordance with societal rules and norms, both legal and ethical.

Friedman is not saying that business shouldn’t be conducted in ethical ways, he even claims that it might “be in the long-run interest of a corporation that is a major employer in a small community to devote resources to providing amenities to that community or to improving its government. That may make it easier to attract desirable employees, it may reduce the wage bill or lessen losses from pilferage and sabotage or have other worthwhile effects” (Kinsley et.al, 2008, p.294). Though, Friedman is clear on that such actions shouldn’t be mislabelled as social responsibility, when goodwill creation is a by-product of expenditures that can be justified entirely in its own self interest (ibid).

Interpreted in a Friedman channel of thought, “being socially responsible” in the following quote would therefore be nothing more than acting in pure self-interest, in line with Friedman’s views (and therefore not really being socially responsible, merely egoistic): “*At its grass roots, being socially responsible has been a concern very much related to the rationale that businesses are more likely to do well in a flourishing society than in one that is falling apart*” (McIntosh et al, 1998 in Brønn, 2001; p. 209)

Therefore, executives making decisions on behalf of the corporation to act “socially responsible” (supporting social causes that ideally should be addressed by government, financed through taxes) will actually reduce the stockholders returns and unnecessarily spend their money, something that some neo-liberalists consider to be mismanagement of the corporation. If the executive on an individual basis wants support social causes and act in a responsible manner, this is very different, as the executive in these incidents will be the principal devoting his own time and money (not the money of his employers). Friedman also realizes that there are some corporations that are founded for eleemosynary purposes (private hospitals or schools) that might not have profits as the main objective, and that the debate is different for these organizations. The same also applies for the individual proprietor, where spending his business’ money on social causes is the same as spending his own money, something that would be in his right to do as the rightful owner of the business.

### 3.1.2 The Stakeholder Perspective – Edward Freeman’s view on CSR

A view that often has been described as contrary to Milton Friedman is Edward Freeman’s stakeholder approach to strategic management and CSR.

As defined by Freeman (1984, p. 47), a stakeholder is “any group of individuals [which] can affect or is affected by the achievement of the organization’s objectives.” Examples of stakeholders include persons within the organization, external groups, neighbourhoods, other organizations, and the environment (Mitchell, Wood, & Agle, 1997).

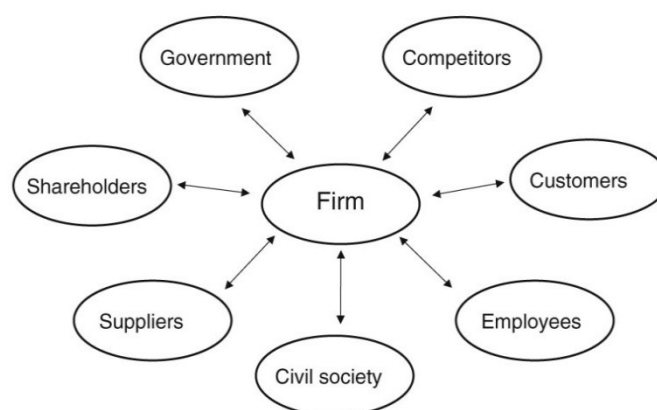


Figure 1. The original stakeholder model – Freeman (1984).

Figure 4 – Freeman’s original stakeholder model

David Vogel (Vogel, 2005) claims that CSR should be best understood as a niche rather than a generic strategy, in some circumstances it makes business sense for some firms in some areas. Further, Vogel maintains that there is a place in the market economy for responsible firms, but that there is also a large place for their less responsible competitors (Vogel, 2005, p. 3).

In Vogel's opinion, CSR reflects both the strengths and shortcomings of market capitalism: "On the one hand, it promotes social and environmental innovation by business, prompting many firms to adopt new policies, strategies, and products, many of which create social benefits and some of which even boost profits by reducing costs, creating new markets, or improving employee morale. Perhaps most important, it enables citizens to both express their own values and possibly influence corporate practices, by "voting" their social preferences through what they purchase, whom they are willing to work for, and where they invest. This politicization of the market can also help shape public debate and public policy.

On the other hand, precisely because CSR is voluntary and market-driven, companies will engage in CSR only to the extent that it makes business sense for them to do so. Civil regulation has proven capable of forcing *some* companies to internalize *some* of the negative externalities associated with *some* of their economic activities. But CSR can reduce only some market failures. It often cannot effectively address the opportunistic behaviours such as free riding that can undermine the effectiveness of private or self-regulation. Unlike government regulation, it cannot force companies to make unprofitable but socially beneficial decisions. In most cases, CSR only makes business sense if the costs of more virtuous behaviour remain modest. This imposes an important constraint on the resources that companies can spend on CSR, and limits the improvements in corporate social and environmental performance that voluntary regulation can produce" (Vogel, 2005, p. 23)

There are different motivations for why companies commit to socially responsible practices; in the same way as human beings has several different motivations that affect behaviour and performance (as described in chapter 2). If one assume that the same motivational theories are applicable for describing why corporations are socially responsible (or not), this behaviour can be categorized into the following areas:

- i) Profitable CSR in pure economic self-interest (economic motivation)
- ii) CSR according to social norms - legal and ethical compliance, the company is not doing anything wrong (social motivation)
- iii) CSR because the actions feel good (intrinsic motivation)
- iv) CSR as a way to help others (moral motivation – pure altruism)
- v) No CSR at all (not profitable) - narrow economic self-interest

These categories help to structure the CSR-debate, and also indirectly imply that corporations will not always act in accordance with economic rationality, and that their self-interest (or their executives' and owners' self-interest) isn't always purely economical. Since human beings have widened, enlightened self-interest consisting of social, moral and intrinsic motivations in addition to their economic motivation, so can corporations (since they are run and owned by people). The motivation behind CSR can also be a mix of these – they are not mutually exclusive.

Companies promoting themselves as socially responsible are perceived more positively and trusted more (integrity and credibility). However, if the company is accused of behaving non-socially, the more positive perception and trust disappear. When consumers are exposed to negative information about a company, consumers seems to trust companies promoting themselves as socially responsible even less than companies not using CSR elements in their communication campaigns (Swaen & Vanhamme, 2004)

As people are different, so are companies, and there will always be debate around how far companies should go in their support for social, cultural and environmental causes. And there is probably not just **one** correct answer to this debate either.

### 3.1.3 Strategy and Society – CSR and competitive advantage

In Michael Porter and Mark Kramers article “Strategy and Society” in Harvard Business Review December 2006, it is claimed that philanthropic initiatives and corporate social responsibility almost never is measured in terms of impact (but in terms of dollars or volunteer hours spent), and that CSR efforts have not been nearly as productive as they could be for two reasons:

- The relationship between Business and Society is traditionally seen as a zero-sum game, focusing on the tension between the two rather than their interdependence.
- Companies are pressured to think about CSR in generic ways rather than the way most appropriate to each firm's strategy

Porter and Kramer are convinced that CSR can become a source of tremendous social progress when looked at strategically, as the business applies its considerable resources, expertise and insights to activities that benefit society. There has been a substantial growth in CSR ratings and rankings, and measuring and publicizing social performance is a potentially powerful way to influence corporate behaviour, especially if such ratings accurately reflect corporate social impact and are consistently measured. According to Porter and Kramer, neither of these conditions unfortunately hold true in the current profusion of CSR checklists (2006, p. 81)

Going back to the starting point for CSR, there are four classical arguments for CSR:

1. *Moral obligation* – companies have a duty to be good citizens and do the right thing. This is illustrated in the goal of the organization Business for Social Responsibility. It asks that its members “achieve commercial success in ways that honor ethical values and respect people, communities, and the natural environment”.
2. *Sustainability* – meeting the needs of the present without compromising the ability of future generations to meet their own needs. Enlightened self-interest, invoking the triple bottom line, securing long-term economic performance through “sustainable strategies and decisions”. But, the sustainability school raises questions about short- vs. long-term trade-offs without offering a framework to answer them.
3. *License to operate* – every company needs tacit or explicit permission from governments, communities, and numerous other stakeholders to do business. Social issues matter to stakeholders, and companies seek to satisfy them and by that give control of their CSR agendas to outsiders.



4. *Reputation* – CSR initiatives will improve a company's image, strengthen its brand, enliven morale, and even raise the value of its stock. This also leads to a focus on external audiences, potentially confusing PR with actual social impact.

A common trait for these four arguments is that they are all generic and focus on the tension between business and society rather than on their interdependence. A successful corporation need a healthy society, and a healthy society needs successful companies (Porter and Kramer, 2006; p. 81-83). A corporate social agenda should look beyond external expectations to find opportunities where social and economic benefits can be achieved simultaneously. This reinforces corporate strategy by advancing social conditions rather than just mitigating harm and meeting community demands.

These observations lead us to the difference between *Responsive CSR* and *Strategic CSR*:

Responsive CSR:

- i) Acting as a good corporate citizen attuned to the evolving concerns of stakeholders
- ii) Mitigating existing or anticipated adverse effects from business activities

Strategic CSR:

- i) CSR beyond best practices. Choosing a unique position and doing things differently from competitors in a way that lowers costs or better serves a particular set of customer needs.
- ii) Involves both inside-out and outside-in dimensions, finding opportunities for creating real shared value and win-win situations.

Shared value is a keyword – a company should identify social issues that intersect with the business. The more closely tied, the greater the opportunity to leverage the firm's resources and benefit society - create shared value. Porter and Kramer (2006, pp. 84-85) identifies a framework with three categories of social issues that affects a company, and that should be sorted and ranked in terms of potential impact:

- i) *Generic social issues*: Important to society but neither significantly affected by the company's operations nor influence the company's long term competitiveness

- ii) *Value chain social impact*: Social issues significantly affected by a company's activities in the ordinary course of business.
- iii) *Social dimensions of competitive context*: Social issues in the external environment that significantly affect the underlying drivers of a company's competitiveness in the locations where it operates.

As for any strategy, a unique value proposition is key – covering a set of customer needs that you can meet but your competitors cannot. The most strategic CSR occurs when a company adds a social dimension to its value proposition, making social impact integral to the overall strategy. An example of this is when Microsoft spends millions of dollars, training jobless American citizens in IT-literacy, and actually ending up hiring many of these. From this, tangible consequences for businesses will be the need to shift away from an emphasis on image to an emphasis on substance. Social impact is first and foremost what needs to be measured, not stakeholder satisfaction. In new CSR strategy, choosing which social issues to focus on is more important than ever if one wants to generate more benefit to both business and society. Porter and Kramer (2006, p. 92) encourage NGOs, governments and companies to stop thinking in terms of “corporate social responsibility” and start thinking in terms of “corporate social integration”. They would also like each company to find out which particular set of societal problems it is best equipped to resolve and where it can gain the greatest competitive advantage, and their conclusion is that “addressing social issues by creating shared value will lead to self-sustaining solutions....a well-run business can have a greater impact on social good than any other institution or philanthropic organization”(ibid).

### 3.1.4 Corporate Social Initiatives

Corporate Social Initiatives is a term Kotler and Lee (2005, p.3) use to describe major efforts under the corporate social responsibility umbrella, and is defined as “major initiatives undertaken by a corporation to support social causes and to fulfil commitments to corporate social responsibility”.

Kotler and Lee mention several causes that are most often supported through corporate social initiatives, such as contributions to community health, poverty, hunger, safety, education,

employment, the environment, local economic development, and other basic human needs and desires. This concept is therefore merely a sub-category of corporate social responsibility, but not stating whether such initiatives will or should have a positive return on investment or not.

### 3.1.5 Corporate Citizenship

“There is no way to avoid paying serious attention to corporate citizenship: the costs of failing are simply too high. ... There are countless win-win opportunities waiting to be discovered: every activity in a firm’s value chain overlaps in some way with social factors—everything from how you buy or procure to how you do your research—yet very few companies have thought about this. The goal is to leverage your company’s unique capabilities in supporting social causes, and improve your competitive context at the same time. The job of today’s leaders is to stop being defensive and start thinking systematically about corporate responsibility.”<sup>5</sup>

- Michael Porter -

The Michael Porter-quote above doesn’t really diverge from the views of Milton Friedman. Porter is talking about win-win opportunities and improving the company’s competitiveness in the same breath as corporate citizenship, something Milton Friedman would claim is pure corporate self-interest, not really “corporate responsibility”.

From the definitions of Corporate Citizenship in Table 3 on next page, it is evident that there are not enormous differences between corporate social responsibility and corporate citizenship. CSR Wire for example defines corporate citizenship as “*companies taking into account their complete impact on society and the environment, not just their impact on the economy. It is about business assuming responsibilities that go well beyond the scope of simple commercial relationships.*”

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<sup>5</sup> Business and Society Conference on Corporate Citizenship, University of Toronto, Rotman School of Management April 2005 (Hohnen & Potts, 2007)

Corporate Citizenship takes the stakeholder approach to strategic management into consideration (and thus goes further into this direction than corporate social responsibility, which in its purest form is defined as a corporation meeting its legal, ethical, commercial and public expectations). Corporate Citizenship is more so defined through a corporation's impact and responsibility towards society and the environment, as well as the economy – realizing that the corporation has stakeholders everywhere it operates (sometimes only limited by the boundaries of the planet itself). This is aligned with the ideas of *sustainable development* and *triple bottom line* thinking.

Definitions of Corporate Citizenship	
(Stebbins, 2001, p. 232)	“Corporate Citizenship is about the belief that companies need to take an active responsibility for their employees’ lives and that corporations have social responsibilities even when meeting those responsibilities may cost money.”
(CCRU (Corporate Citizenship Research Unit) at Deakin University in Australia, 2005)	“Corporate Citizenship is a recognition that a business, corporation or business-like organisation has got social, cultural and environmental responsibilities to the community in which it seeks a licence to operate, as well as economic and financial ones to its shareholders or immediate stakeholders. Corporate citizenship involves an organisation coming to terms with the need for, often, radical internal and external changes, in order to better meet its responsibilities to all of its stakeholders (direct or indirect), in order to establish, and maintain, sustainable success for the organisation, and, as a result of that success, to achieve long term sustainable success for the community at large.”
(The Center for Corporate Citizenship at Boston College., 2005)	“Corporate citizenship is the business strategy that shapes the values underpinning a company’s mission and the choices made each day by its executives, managers and employees as they engage with society.”
(CSR Wire)	“Corporate Citizenship is about companies taking into account their complete impact on society and the environment, not just their impact on the economy. It is about business assuming responsibilities that go well beyond the scope of simple commercial relationships.”

Table 3 - Definitions of Corporate Citizenship

### 3.1.6 Corporate Philanthropy

Philanthropy is defined in Wikipedia as “the act of donating money, goods, services, time and/or effort to support a socially beneficial cause, with a defined objective and with no financial or material reward to the donor. In a more general sense, philanthropy may encompass any altruistic activity intended to promote good or improve human quality of life. One who practices philanthropy may be called a *philanthropist*”. Corporate philanthropy is merely the corporate version of philanthropy – “a direct contribution by a corporation to a charity or cause, most often in the form of cash grants, donations and/or in-kind services” (Kotler & Lee, 2005, p. 144). Lerner and Fryxell (1988, in Brønn, 2001) define corporate philanthropy as “an activity above and beyond what is required of an organization and which can have a significant impact of the communities in which a company operates.”

Of the different corporate social initiatives, corporate philanthropy might historically be the most traditional of them all, with billions of dollars going to human services, culture and the arts, education, environmental protection, local and global communities and health related issues. The corporate donations are often critical to cover the gap between expenses and revenues in countless nonprofit organizations, critical to their annual revenue stream (ibid).

According to Kotler and Lee, corporate philanthropy has matured over the decades as a response to internal and external pressures to balance concerns for shareholder wealth with concerns for responsibilities in the communities where the corporation operates. This has led to five different responses:

- i) A more strategic approach to selecting social issues to support
- ii) More long-term relationships with non-profit organizations
- iii) More options for giving (beyond cash) – products, expertise, distribution..
- iv) Employee involvement in selection process for philanthropic programs
- v) Giving now also includes international communities where corporations are doing business

Benefits of corporate philanthropy can be increased goodwill and better brand image, and Porter and Kramer (The Competitive Advantage of Corporate Philanthropy, 2002) also claim that philanthropy can be one of the most cost-effective ways for a company to improve its

competitive context – the quality of the business environment in the locations where they operate. They argue that philanthropic activities can and should go beyond generating goodwill, and actually enhance a company's productivity.

The greatest concerns with corporate philanthropy are the challenges associated with evaluating and choosing a strong cause partner, dealing with shareholder concerns for issues that have been selected, achieving positive visibility for the corporation for its efforts, and tracking and measuring impact and outcomes (Kotler & Lee, 2005, p. 174).

### 3.1.7 Criticism of Corporate Social Responsibility

A lot of the criticism towards Corporate Social Responsibility was presented in 3.1.1, where Milton Friedman states that a business is not a person and cannot therefore have any responsibilities. Any spending on CSR outside of acting in the best interest of the shareholder (often maximizing profits) could therefore be seen as misconduct of the business. With a focus on the shareholders' best interest and profit maximization, CSR is reduced to nothing but enlightened self-interest. It can be claimed that CSR rarely has got anything to do with altruism (but social norms that pressures these companies to act "good", or that business leaders see that they can increase profits by taking actions in the "social sphere" into consideration).

If CSR happens to be motivated by altruism, doesn't it then take away from the profit maximization of a company – spending money on something that could be said to be irrelevant for running the business? It is here Michael Porter and Mark Kramer claims that one should not spend CSR-money on causes that are not a strategic fit with the core offering of the company.

And when all comes down to the end of the year – what is the *real social impact* of CSR? Are corporations in the private sector really changing the world towards the better? There is no doubt that there are many good stories told in new, flashy sustainability or triple bottom line reports coming out alongside the annual reports. Unfortunately, these reports are often not too focused on actual social impact, but on storytelling and brand-building.

## 3.2 Cause Related Marketing (CRM)

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In the US, corporate spending on cause related marketing jumped from \$125m in 1990 to \$828m in 2002 (Brand Strategy, 2003). A classic example of CRM was the restoration of the Statue of Liberty in the 1980s. American Express pledged to donate 1 cent toward the restoration project for each time a transaction was made by its cardholders. This cause-marketing effort resulted in a \$1.7 million donation by American Express to the restoration project and a 28 percent increase in credit card usage by American Express cardholders, creating a win-win situation.

Cause related marketing is defined by Mullen (1997, in Brønn, 2001) as the process of formulating and implementing marketing activities that are characterized by contributing a specific amount to a designated non-profit effort that, in turn, causes customers to engage in revenue-providing activities.

Sue Adkins and the organization “Business in the Community” defines Cause Related Marketing as “a commercial activity by which business and charities or causes form a partnership with each other to market an image, product or service for mutual benefit” (Adkins, 1999). This definition is wider than the one Mullen uses, where it is mentioned that a specific amount must be contributed, coming from customer sales. Adkins feels CRM should be defined wider than “purely a sales promotion” (1999, p.10), where one also takes all the marketing aspects into consideration; advertising, public relations, direct marketing, sponsorship, direct mail, strategic brand building and more. Her point is that all the aspects of the marketing mix apply to CRM, and that the main points where definitions differ is in the interpretation of the immediacy of the impact on the bottom line.

Kotler and Lee (2005, pp. 81-82) use a similar description of CRM as Mullen, where “a corporation commits to making a contribution or donating a percentage of revenues to a specific cause based on product sales. Most commonly this offer is for an announced period of time and for a specific product and a specified charity. This link to *product sales* or transactions most distinguishes this initiative, which contains a mutually beneficial

understanding and goal that the program will raise funds for the charity and has the potential to increase sales for the corporation”.

Cause-related marketing is a marketing initiative where the corporate contribution levels usually are dependent on some consumer action, unlike most of the other corporate social initiatives out there. In cause-related marketing, consumer response is an essential part of the campaign, and will eventually determine the success of the campaign. It usually also involves a more formal relationship with one or more charitable organizations, to create mutually beneficial situation for both parties involved.

A wide range of causes are supported by cause-related marketing campaigns, but the most visible ones are associated with major health issues (e.g. cancer, AIDS, heart disease), children's needs (education, hunger, orphans), basic local and global needs (hunger, homelessness, community issues) and the environment (nature, wildlife, climate change).

A corporation's benefits from cause-related marketing can be (Kotler & Lee, 2005, p. 84) :

- Raising funds for a cause
- Attracting new customers
- Reaching niche markets
- Increasing product sales
- Building positive brand identity

According to Sue Adkins (1999), CRM is no more than enlightened self-interest. The company uses CRM to raise money for a cause but at the same time promoting its image, products and services in conjunction with this good cause – enhancing the company's reputation, showing off its values, and building a more loyal customer base. Adkins neither sees CRM as philanthropy nor as altruism. She claims the parties enter a CRM-relationship to receive a return on their investment, a return that gains both partners. Both the charity and the business are looking to enhance their brand reputation, increase customer traffic, get positive PR or increase income or resources (1999, p. 12).

It is a “dramatic way to build brand equity ... as it creates the most added value and most directly enhances financial performance” (Mullen, 1997, in Brønn, 2001). It can generate the



long-term value needed for a company to survive and achieve competitive advantage (Collins, 1993 in Brønn, 2001), and is seen as a way for companies to establish long-term differentiation from competitors and add value to the corporate brand (Davidson, 1997 in Lafferty et al. 2004) An effective cause related marketing program can create a triple win situation: – namely a win for the business, a win for the cause or charity and a win for the consumer.

A study by Lafferty et al (2004) looks into the consequences of cause related marketing campaigns on both the attitudes towards the cause and the brand before and after the campaign. The results of the study are that attitudes toward both the cause and the brand are enhanced as a consequence of an alliance if perceptions of the alliance itself are favourable. Furthermore, the cause appears to benefit from the alliance to a greater extent than the brand, and fit between brand and cause is essential for consumer acceptance and support. Consequences of these findings are that both parts should be careful before entering into a cause-brand alliance, where familiarity of the cause (and also the brand) can be very beneficial for the alliance. For an unknown company, an alliance with a familiar cause can be quite beneficial. The fit between the cause and the brand also needs to be good, similar to what one see in cobranding literature (ibid).

Another relevant point for CRM is that a consumer's previous active commitment to a cause increases the expected willingness to buy a product related to the cause, but this effect only works when the cost associated with supporting the cause is minimal (e.g. the consumer doesn't have to make additional donations towards the cause himself/herself, the donation is taken care of by the corporation through the sales of the product) (Vaidyanathan & Aggarwal, 2005). In other words – the cause related marketing needs to be done in the right way, making it as easy and convenient for the consumer to participate in the campaign.

### 3.2.1 Concerns with CRM

There are also several concerns with CRM, some unique to this phenomenon and others are common challenges associated with corporate social initiatives in general. Some of the main concerns are:

- The Cause-Brand Alliance is a more complicated agreement than most other social initiatives (contractually closer to a small version of a joint venture)
- Increased needs (relative to other social initiatives). Tracking systems, crediting the cause after sales etc.
- Participation levels need to be high in order for the effort to be worthwhile, since the per item donations are often small.
- Some consumers are skeptical to the charity/cause the brand is being associated with, and might not want to purchase the product as a result. This might hurt the brand.
- Good marketing and promotional executions are necessary to get the full effect from the campaign. This can often be more expensive than the campaign itself.
- Skepticism from consumers to campaigns like these (more so than towards corporate philanthropy in general). According to Webb and Mohr (1998, in Brønn, 2001) many consumers are skeptical towards CRM-initiatives and the implementation of these and/or showing cynicism towards a firm's motives. People sometimes think that companies are trying to buy their way out of negative situations through CRM. The best way to decrease this skepticism is to first of all understand where it is coming from, and then increase the customer's knowledge about the campaign. Clearly communicating the term of the offer and the results from the campaign as it progresses helps to create a trustworthy initiative. Honesty, long-term commitment to a cause and involvement of non-profit organizations are key factors in overcoming skepticism towards CRM. Understanding how the public perceive companies and what they expect in return for their support is essential (ibid).

### 3.3 The Triple Bottom Line

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The term “the triple bottom line” (TBL/3BL/ People, Planet, Profit) was coined by John Elkington in his 1997 book *Cannibals with Forks*. It is meant to “focus corporations not just on economic value, but also on the environmental and social value they add – and destroy. At its narrowest, the term triple bottom line is used as a framework for measuring and reporting corporate performance against economic, social and environmental parameters” (SustainAbility).

Companies are talking about creating a “positive” ROI on all three bottom lines (a “positive” 3BL), as well as creating benefits for all stakeholders. The triple bottom line is meant to measure the impact of an organization’s activities on the world. Though, there are currently few standards for actually measuring these impacts objectively. Savitz and Weber (2006) are trying to explain these issues by comparing triple bottom line reporting to financial reporting:

*“Just as meaningful financial reporting cannot be reduced to one number, so sustainability does not sum precisely. There is yet no way to accurately or completely describe consumer benefits or community benefits using a number, and some numbers themselves require a great deal of explanation, which is precisely why most financial reports include pages of management discussion and analysis. The Triple Bottom Line exists currently as a kind of balanced scorecard that captures in numbers and words the degree to which any company is or is not creating value for its shareholders and for society.”*

The idea behind the triple bottom line is noble – trying to refocus corporations to think about and measure more than just the financials, where social issues and environmental issues are seen as equally important as the financial performance. It is clearly inspired by the sustainability agenda (described in chapter 2), and is very much aligned with Freeman’s stakeholder theory (described earlier in this chapter). The term “triple bottom line” should be placed as a sub-category within corporate social responsibility, where the novelty of the concept is its impact-focused approach to planning, measuring and reporting on these issues. It is not much more than a refocused CSR stakeholder and sustainability theory, where a corporation’s environmental impact is reconstructed as its own category of equal importance to financial performance and overall social impact.

A valid question towards John Elkinton’s conceptualization of the triple bottom line could certainly be why he chose to elevate the environment as a 1/3 of this concept, as an equally important category as all other social issues aggregated. Preserving the environment is obviously very important and an essential part of creating a sustainable future, but in the Brundtland Commission’s original definition of sustainability from 1987 it was identified that the needs of the world’s poor should be given overriding priority.

### 3.3.1 Criticism of the triple bottom line

First of all, the criticism towards stakeholder theory will also apply to the triple bottom line. Is it really the private sector's responsibility to create a ***positive ROI*** for the environment and society, regardless of what their key competences are? One thing is not exploiting people and the planet (*not having a negative impact*), another thing is how much that should be given back to people and the planet in general, especially in situations when creating a "positive ROI" for environmental and social issues equals a negative impact on the financial bottom line. *Not having a negative impact* VS *positive impact* represents two very different ethical positions, where not having a negative impact can be seen as satisfactory and not doing anything wrong, whereas a positive ROI can be considered as above and beyond what is expected in the profit maximizing private sector. This does not mean that there isn't room for companies and organizations that go above and beyond, just that this cannot be expected to happen all the time in the profit maximizing private sector. Also, what can be observed up to date is that many companies have started to report on the triple bottom line, but then more so on how they are taking actions to avoid the *negative impact* on people and the planet, in terms of environmentally neutral practices (usually called environmentally *friendly* practices) and fair trade. Some would though claim that fair trade and environmental neutrality should be a bare minimum for how companies operate, but this reality is unfortunately far away; even eliminating the *negative impacts* private sector has on the world has proven more difficult than it should be.

In their 2003-article "Getting to the bottom of triple bottom line", Wayne Norman and Chris MacDonald critically examine the notion of triple bottom line-accounting. They criticise the concept triple bottom line for not really bringing anything new to the corporate social responsibility-discussion, and that what could have been new and a useful addition to the field (measuring and reporting – on the social and environmental bottom lines, with a net social and environmental profit/loss) is untenable. It currently does not exist an easy, objective (and universally accepted) way to measure social and environmental performance – something that makes the entire concept open for subjective interpretation. Norman and MacDonald claims that the triple bottom line rhetoric of bringing accounting paradigms into the social and environmental domains is "badly misleading, and may in fact provide a smokescreen behind which firms can avoid truly effective social and environmental reporting

and performance”. To Norman and MacDonald, it doesn’t make sense to talk about a social and environmental bottom line until there is a universally accepted methodology that allows us to add and subtract data arriving at a net sum (similar to financial methodology). The closest anyone has come to proposing anything like this might be the B-Corporation certification system (B Corporation.net), assessing a company’s overall stakeholder impact, grading it from 0-210 weighted points, where you need a minimum of 80 points to become a certified B-Corporation.

## Chapter 4 – Trends and concepts related to financial value creation in the social sector

This chapter will discuss “social entrepreneurship” and “social business”, two major trends where elements of business operations and financial value creation are blended into nonprofit organizations. These two concepts are getting increased attention in media, conferences and business schools all over the world, and are the two most important areas when describing current reforms and movements in the social sector - since the social sector has realized that it cannot depend fully on donations, grants and other philanthropic contributions to survive – it is too volatile.

Especially part 4.2 (Social Business) will be useful for categorizing four different types of enterprising nonprofits, proving the nonprofit convergence towards the private sector:

- i) No cost recovery
- ii) Some cost recovery
- iii) Full cost recovery
- iv) More than full cost recovery

### 4.1 Social entrepreneurship

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*“Social entrepreneurship is attracting growing amounts of talent, money, and attention. But along with its increasing popularity has come less certainty about what exactly a social entrepreneur is and does. As a result, all sorts of activities are now being called social entrepreneurship.”*

- Martin & Osberg, Stanford Social Innovation Review (2007)

The emerging field of social entrepreneurship and social enterprise is growing larger and becoming more popular than ever, with new conferences, foundations and entire educational programmes dedicated to describe and develop this phenomenon. The idea of social entrepreneurship is well suited to our times, mixing the two powerful elements of social passion and innovative business practices. There is both a need and demand for new,

entrepreneurial approaches to social problems, and an accompanying supply of emerging social entrepreneurs.

According to J. Gregory Dees (Dees, 1998) the new name social entrepreneurship is important in that it implies a blurring of sector boundaries. He further states that: *“Though the concept of “social entrepreneurship” is gaining popularity, it means different things to different people. This can be confusing. Many associate social entrepreneurship exclusively with not-for-profit organizations starting for-profit or earned-income ventures. Others use it to describe anyone who starts a not-for-profit organization. Still others use it to refer to business owners who integrate social responsibility into their operations”* (Dees, 1998, p.1).

In his 1998-article, “The Meaning of Social Entrepreneurship”, J.Gregory Dees discusses what the concept “social entrepreneurship” really means, and starts by going back to the roots of the term entrepreneurship and Joseph Schumpeter’s discussions of the concept in “The Theory of Economic Development” from 1934. According to Schumpeter, entrepreneurs are the innovators driving the “creative-destructive” process of capitalism:

*“The function of entrepreneurs is to reform or revolutionize the pattern of production.” They can do this in many ways: “by exploiting an invention or, more generally, an untried technological possibility for producing a new commodity or producing an old one in a new way, by opening up a new source of supply of materials or a new outlet for products, by reorganizing an industry and so on.”* (Schumpeter, 1934 in Dees, 1998)

In other words, entrepreneurs are drivers of change, moving the economy forward by finding new ways of solving old problems or meeting unmet needs. Social entrepreneurs are very similar – but their mission is focused around solving social issues and creating social impact where there is a social need, more so than creating wealth. J. Gregory Dees definition of social entrepreneurship is:

*“Play the role of change agents in the social sector, by:*

- 1) Adopting a mission to create and sustain social value (not just private value),*
- 2) Recognizing and relentlessly pursuing new opportunities to serve that mission,*
- 3) Engaging in a process of continuous innovation, adaptation, and learning,*
- 4) Acting boldly without being limited by resources currently in hand, and*

*5) Exhibiting heightened accountability to the constituencies served and for the outcomes created”*

A range of other definitions of the concept can be found in Table 4 below.

Source	Definition of Social Entrepreneurship
Leadbetter (1997)	The use of entrepreneurial behavior for social ends rather than for profit objectives, or alternatively, that the profits generated from market activities are used for the benefit of a specific disadvantaged group.
Thake and Zadek (1997)	Social entrepreneurs are driven by a desire for social justice. They seek a direct link between their actions and an improvement in the quality of life for the people with whom they work and those that they seek to serve. They aim to produce solutions which are sustainable financially, organizationally, socially and environmentally.
Dees (1998)	Play the role of change agents in the social sector, by: 1) Adopting a mission to create and sustain social value (not just private value), 2) Recognizing and relentlessly pursuing new opportunities to serve that mission, 3) Engaging in a process of continuous innovation, adaptation, and learning, 4) Acting boldly without being limited by resources currently in hand, and 5) Exhibiting heightened accountability to the constituencies served and for the outcomes created.
Reis (1999) (Kello gg Foundation)	Social entrepreneurs create social value through innovation and leveraging financial resources...for social, economic and community development.
Fowler (2000)	Social Entrepreneurship is the creation of viable socio-economic structures, relations, institutions, organizations and practices that yield and sustain social benefits.
Brinkerhoff (2001)	Individuals constantly looking for new ways to serve their constituencies and add value to existing services
Mort et al. (2002)	A multidimensional construct involving the expression of entrepreneurially virtuous behavior to achieve the social mission...the ability to recognize social value creating opportunities and key decision-making characteristics of innovation, proactiveness and risk-taking
Drayton (2002)	A major change agent, one whose core values center on identifying, addressing and solving societal problems.
Alford et al. (2004)	Creates innovative solutions to immediate social problems and mobilizes the ideas, capacities, resources and social arrangements required for social transformations
Harding (2004)	Entrepreneurs motivated by social objectives to instigate some form of new activity or venture.
Shaw (2004)	The work of community, voluntary and public organizations as well as private firms working for social rather than only profit objectives.
Said School (2005)	A professional, innovative and sustainable approach to systematic change that resolves social market failures and grasps opportunities
Fuqua School (2005)	The art of simultaneously pursuing both a financial and a social return on investment (the “double” bottom line)
Schwab	Applying practical, innovative and sustainable approaches to benefit society in



Foundation (2005)	general, with an emphasis on those who are marginalized and poor.
NYU Stern (2005)	The process of using entrepreneurial and business skills to create innovative approaches to social problems. "These non-profit and for profit ventures pursue the double bottom line of social impact and financial self-sustainability or profitability."
MacMillan (2005) (Wharton Center)	Process whereby the creation of new business enterprise leads to social wealth enhancement so that both society and the entrepreneur benefit.
Tan et al. (2005)	Making profits by innovation in the face of risk with the involvement of a segment of society and where all or part of the benefits accrue to that same segment of society.
Mair and Marti (2006a)	...a process of creating value by combining resources in new ways...intended primarily to explore and exploit opportunities to create social value by stimulating social change or meeting social needs.
Peredo and McLean (2006)	Social entrepreneurship is exercised where some person or group....aim(s) at creating social value...shows a capacity to recognize and take advantage of opportunities...employ innovation...accept an above average degree of risk...and are unusually resourceful ...in pursuing their social venture.
Martin and Osberg (2007)	Social entrepreneurship is the: 1) identification a stable yet unjust equilibrium which the excludes, marginalizes or causes suffering to a group which lacks the means to transform the equilibrium; 2) identification of an opportunity and developing a new social value proposition to challenge the equilibrium, and 3) forging a new, stable equilibrium to alleviate the suffering of the targeted group through imitation and creation of a stable ecosystem around the new equilibrium to ensure a better future for the group and society.

Table 4 - Definitions and descriptions of social entrepreneurship and social entrepreneurs. (Zahra, Gedajlovic, Neubam, & Shulman, 2006)

As the table above shows, the definitions of social entrepreneurship substantially differ. The definitions vary both in content and approach; some are process-based, others are entrepreneur-centric, and they vary quite much in regards to how much they include business enterprise and business skills as a component of social entrepreneurship.

#### 4.1.1 Criticism of social entrepreneurship

*"The phrase social entrepreneurship is hugely overused right now. It seems that everybody who is doing anything the least bit creative for the public good is now being called a social entrepreneur. Once a term gets a certain amount of status or excitement associated with it, then everybody applies it."*

David Bornstein in (Harrison, 2006, p. 59)

According to Roger Martin and Sally Osberg (2007, p. 30), “the actual definition of what social entrepreneurs do to produce this order of magnitude return is less clear than the potential benefits offered... ..in fact, the definition of social entrepreneurship today is anything but clear. As a result, social entrepreneurship has become so inclusive that it now has an immense tent into which all manner of socially beneficial activities fit.”

One can claim that the term social entrepreneurship is not really that different from “regular” entrepreneurship, whose purpose is not really first and foremost to create wealth, but to find new solutions to existing problems and needs (according to Schumpeter’s original definition from 1934). In fact, most businesses are not founded with the purpose of creating wealth, but to create some kind of product or service that there is a demand and a need for out there. The economic value creation comes as a natural consequence of supplying this product or service where there is a demand, and the same value creation is what allows the corporation to grow and create more jobs and new products and services. One can discuss whether the corporation on its own is first and foremost a way of generating social value and bringing humanity to the next level through innovations and change. By taking a look back in history, it is obvious that the capitalistic system has brought hundreds of millions of people out of poverty in a wide range of countries – a system that can be claimed to be one of the most successful and most comprehensive solutions to fighting poverty in history. It is proven that the system works, but at the same time there is no doubt that it needs some adjustments on the way.

## 4.2 Social business

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By being awarded the Nobel Peace Prize in 2006, Dr. Muhammad Yunus opened the eyes of the world to the concepts of “social business” and “social business entrepreneurs”. Yunus suggests to make the current interpretation of capitalism wider, by introducing another kind of business and another kind of people that also works within the capitalistic system – “one that recognizes the multidimensional nature of human beings” (Yunus, 2007, p. 21)

According to Yunus, there are two different types of human beings and businesses in the world:

- i) The *existing type* – profit maximizing businesses (PMB) and people.
- ii) The *new type*, totally committed to making a difference in the world and socially objective driven more so than anything else. This new kind of business is what Yunus refers to as **social business**.

This new business is basically the same as the existing PMB, but with different objectives – to create social benefits for those lives it touches. Like other businesses, it employs workers, creates goods or services and provides these to customers for a price consistent with its objective. Such social businesses are founded by social entrepreneurs.

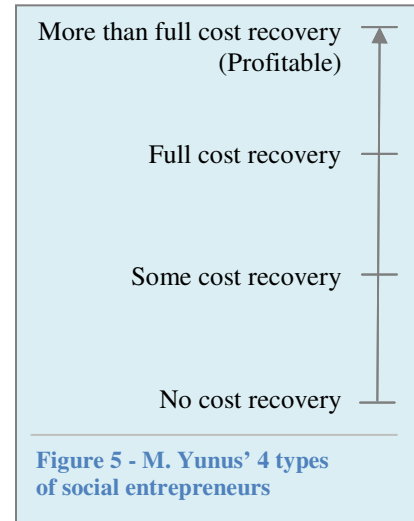
Yunus (Yunus, 2003) describes that not all social entrepreneurs use money to achieve their objectives (but use their time, labour, talent, skill etc. instead), but classifies the social entrepreneur who use money into four types:

- v) No cost recovery
- vi) Some cost recovery
- vii) Full cost recovery
- viii) More than full cost recovery

Yunus further says that “once a social entrepreneur operates at 100% or beyond the cost recovery point, he has entered the business world with limitless possibilities. He has overcome the gravitational force of financial dependence, and this is a critical moment of significant institutional transformation. He has moved from the world of philanthropy to the world of business. To distinguish him from the first two types of social entrepreneurs listed above, we will call him “social business entrepreneur (SBE)”.

Yunus believe that the market place will become more interesting and competitive with the introduction of SBEs, because these new players can be equally aggressive and enterprising in achieving their goals as other businesses. He also thinks that SBEs have got the potential to become powerful players in the national and international economy, but that they have not gotten the recognition in the marketplace that they deserve yet. Yunus asks for room for the SBEs in our conceptual frameworks and that there should be created supporting institutions, policies, regulations, norms and rules for these new, different (but equally competitive?) organizations.

Yunus argues that a social business is not a charity, but a business in every sense, with the need for full cost recovery while achieving its social objective. It needs to be run with the mindset of running a business (2007; 23). Another way a social business differs from a charity or an NGO, is that a social business according to Yunus has owners who are entitled to recoup their investments. But as soon as the social business has paid back its initial loans and starts turning a profit, the surplus generated is reinvested in the business – as a non-loss, non-dividend business providing



social benefit to people in need. Hence, the social business will give back to the ones that it is meant to serve in the first place – the disadvantaged. A social business can also be owned by the people it is meant to serve, like Grameen Bank is owned by the poor. 94% of the ownership shares of Grameen Bank are held by the borrowers themselves (Yunus, 2007; 24).

The typology that Professor Yunus uses to classify social entrepreneurs has clearly got its root in the Non-Profit/Civil Sector, starting off with *No cost recovery* as his first type. A social enterprise with no cost recovery is what we traditionally think about as a charitable organization (with a non-profit motive), relying on philanthropy, donations and grants to conduct its operations. Then Yunus is moving on to *Some cost recovery*, what we can classify as an enterprising non-profit/charitable organization – a charity that starts using some business means to create a revenue stream for itself (though it is still a charity relying on some degree of philanthropic funds to achieve its mission). It is first when we get to *full cost recovery* that these organizations take the step into the world of business, with the ability to compete on same terms as businesses in a financially sustainable way. At this point, the organization does not rely on external philanthropic funding anymore.

#### 4.2.1 Criticism of social business

Coming from the nonprofit side, Yunus doesn't take into consideration anything else than a 100% social purpose model. He creates a dichotomy of *the existing type of business* and the *new type of business*, a dichotomy that is very black and white compared to what the real

world looks like. There are definitely businesses that could be placed in between these two, like Novo Nordisk and the Carlsberg Group, that are owned respectively 25.5% and 30.3% by their foundations (and with 72.9% and 70.5% of the votes because of a structure with A-shares (not in free float) and B-Shares (in free float)). Both the Novo Nordisk Foundation and the Carlsberg Foundation gives out millions of dollars every year to good causes, and govern their companies with a social purpose in mind.

## Chapter 5 – Converging Sectors - Dual Value Creation

The previous chapters made it evident that there are some powerful and relevant changes happening in our world. As a consequence of global structural changes the last two decades and changing values towards more postmaterialism in the “developed” world, there is a movement of people and organizations continuously trying to find better ways to solve some of the most pressing problems humanity is facing globally and locally. There is a multitude of solutions popping up; greater good-solutions that undoubtedly will improve our present and our future. Most of these are new, creative applications of recycled success-stories from the past, and some solutions are as simple as taking the current game to the next level.

On the For-Profit side, business strategies like CSR, corporate citizenship, corporate philanthropy, cause related marketing and triple bottom line-thinking are increasing in popularity (both supply and demand), refocusing businesses towards the social impact they have (at the same time as turning a profit). The social purpose of a business is becoming increasingly important, and for many modern corporations the focus not just around creating economic value anymore. This new duality of social and economic value creation in the private sector leads to innovations in how businesses are structured and how they interact with stakeholders.

On the Non-Profit side, there has been more and more focus on enterprising Non-Profits; Non-Profits that are starting to use commercial tools to create revenue streams to cover their own costs or fund their own social initiatives. This has led to the rise of the social enterprise, a phenomenon where social value creation is the main purpose and economic value creation is the vehicle to achieve this. This is the same duality of value creation as observed in the private sector, but approached from a different angle.

Some very tangible consequences of this is the increased pressure on the existing sectors, where the private sector is increasingly preoccupied with the improvement of their social impact (on top of their financial value creation), and the nonprofit sector is equivalently and increasingly desperate for sustainable revenue streams to free them from their dependency in volatile philanthropic contributions and donations. Combine this with a spoonful of a new breed of socially entrepreneurial creative destructionists, social capitalists eager to benefit the greater good, hardcore businesspeople turning altruist, and the recipe is complete. This new dish is sometimes called strategic CSR, social enterprise, enterprising nonprofits, social business, hybrid companies, for-benefits or the Fourth Sector.

Though, one can claim that this is actually not a new recipe/dish in itself, since there have been examples of organizations using business to benefit the public good ever since the early days of modern humanity. The big difference nowadays is that there are way more people and organizations cooking and eating this dish than ever before. The model of dual social and financial value creation is picking up momentum, and this convergence between the private sector and the social sector points towards the creation of an entirely new sector - a hybrid sector, a for-benefit sector, a fourth sector.

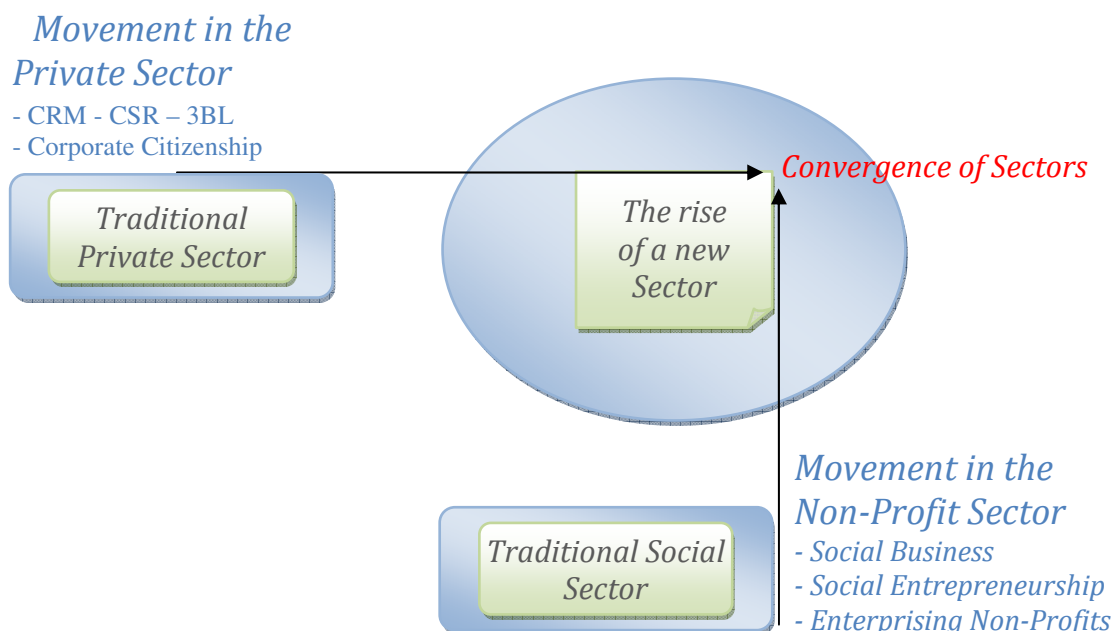


Figure 6 - Convergence of Sectors

## 5.1 Hybrid companies, for-benefits and the fourth sector

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### 5.1.1 Kim Alter's Hybrid Spectrum

In her article from 2004, Kim Alter is describing the blurry field of converging dual-value creating organizations on a spectrum. By using a spectrum, this typology is less black and white than some of the classical debates where the for-profit world (whose *raison d'être* is to create economic value) and the nonprofit world (whose purpose is to create social value) are seen as incompatible opposites.

According to Alter (2004, p. 1), “these dichotomies are increasingly coming together in practice through the application of methods that marry market mechanisms to affect *both* social and economic value resulting in *total* value creation”. She further says that “value creation is the backbone of social enterprise and serves as a fundamental and unifying principle between different social change and economic development approaches. To this end, the typology is not intended to straightjacket practitioners into a prescribed set of formulas, but rather recognize and embrace the abundance of possibility under the umbrella of a larger vision”.

### **The Hybrid Organization**

As we can see in Table 5 below, Hybrid organizations have mixed motives of self-interest and altruism, and generate both economic and social value. They are organized after how they use their income/profits, and are accountable towards all stakeholders. Though, what Alter defines as a hybrid organization, is very similar to many of the definitions of social entrepreneurship seen in Chapter 4.

	Purely Philanthropic	Hybrid	Purely Commercial
Motives	Appeal to goodwill	Mixed motives	Appeal to self-interest
Methods	Mission-driven	Balance of Mission and Market	Market-driven
Goals	Social value creation	Social and economic value creation	Economic value creation
Destination of Income/Profit	Directed toward mission activities of nonprofit organization (required by law or organizational policy)	Reinvested in mission activities, or operational expenses, and/or retained for business growth and development (for-profits may redistribute a portion)	Distributed to shareholders and owners

Table 5 - Spectrum of Practitioners (Alter, 2004)

## Hybrid Spectrum

Besides the purely commercial traditional for-profit, and the purely philanthropic traditional nonprofit, Alter's spectrum includes four types of Hybrid Organizations.

These four types of Hybrid Organizations can again be divided into two distinct families, characteristically separated by their main purpose:

- i) On the left hand side are the for-profit entities whose main purpose according to Alter is to be **profitable** (shareholder return), but that also create some degree of social value.
- ii) On the right hand side of the spectrum are “nonprofits and social enterprises whose main purpose is to create **social impact**, with commercial activities that generate economic value to fund social programs but whose main motive is mission accomplishment as dictated by stakeholder mandate” (Alter, 2004, p. 7).

Commonalities between both sides of the spectrum, is that both types of hybrids pursue strategies of both economic and social value creation to achieve their goals. According to Alter, for-profits incorporate social programs to achieve their profit making objectives, and nonprofits integrate commercial practices to support their social mission.



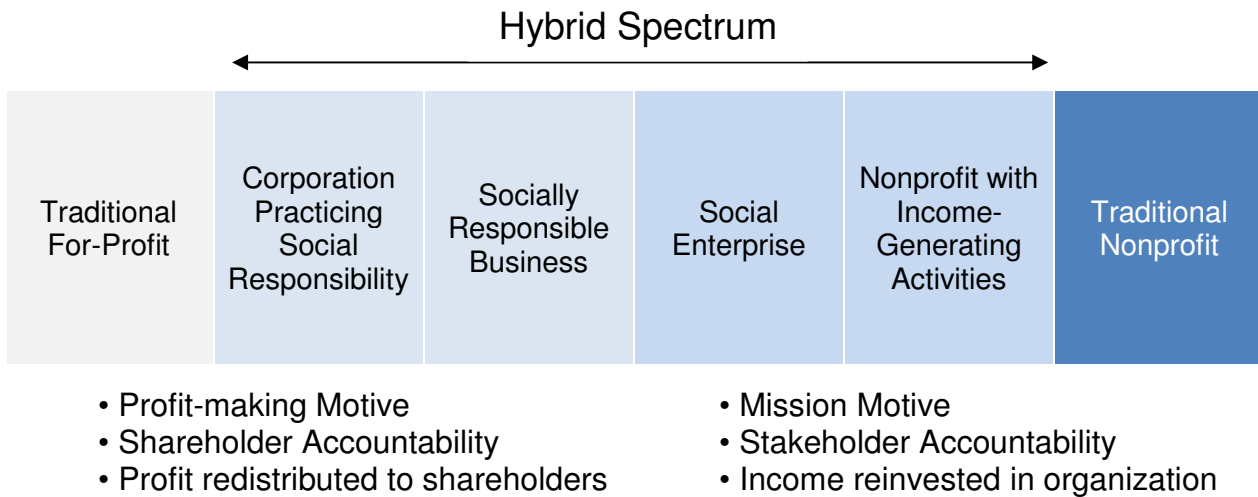


Figure 7 - The Hybrid Spectrum

## The Four types of Hybrid Organizations

1. Corporation practicing social responsibility
2. Socially responsible business
3. Social Enterprise
4. Nonprofit with income-generating activities

These different organizations will be briefly described, using Kim Alter's definitions.

### 1. Corporation Practicing Social Responsibility

Defined by Alter as "For-profit businesses whose motives are financially driven, but who engage in philanthropy. This strategic philanthropy helps companies achieve profit maximization and market share objectives while contributing to public good." (2004, p. 13)

### 2. Socially Responsible Business

This is defined as "For-profit companies that operate with dual objectives - making profit for their shareholders and contributing to a broader social good. Socially responsible businesses are willing to forsake profit or make substantial financial contributions rather than distribute earnings privately, and frequently place social goals in their corporate mission statements" (2004, p. 12).

### 3. Social Enterprise

Kim Alter and Virtue Ventures define social enterprise narrower and closer towards a business than most of the definitions in Chapter 4. Their definition of social enterprise is “*any business venture created for a social purpose – mitigating/reducing a social problem or a market failure – and to generate social value while operating with the financial discipline, innovation and determination of a private sector business.*” (2004, p. 11). This definition is very similar to what Muhammad Yunus defines as a social business in Chapter 4.

Alter further describes three variants of a social enterprise, based on the actual mission orientation of the organization. These three are *i) Mission Centric*, meaning that the enterprising activities directly support the social program of the organization, *ii) Mission Related*, where the business activities have some synergies with or support of the core social program and *iii) Unrelated to Mission*, where the business activities are indirectly related to the social programs and support the social mission with profits or revenue.

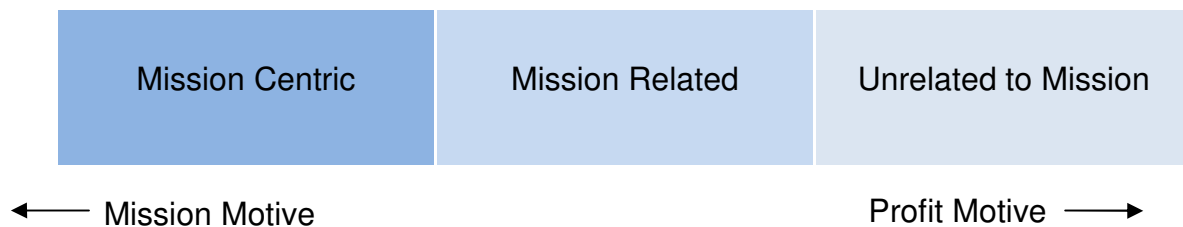


Figure 8 – Social Enterprise mission orientation

These three variants can also be described as in Figure 9 below, where the level of integration between the social programs and the enterprise activities are visualized.

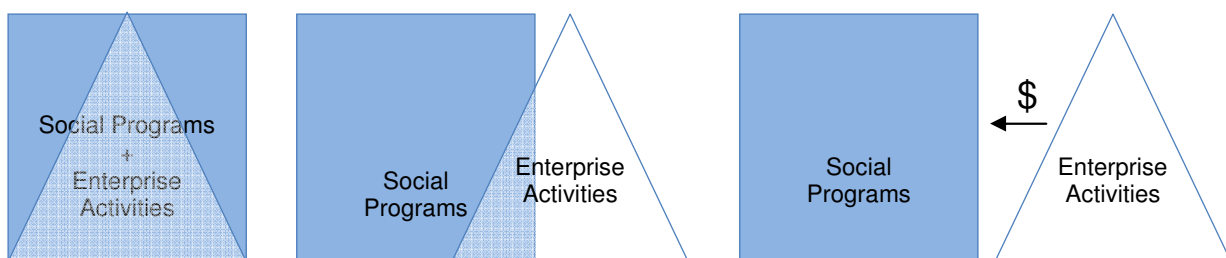


Figure 9 - Level of integration between social programs and business activities

#### **4. Nonprofit with Income-Generating Activities**

This is defined as “Nonprofit organizations that incorporate some form of revenue generation into their operations. Income-generating activities are not conducted as a separate business, but rather are integrated into the organization's other activities. These activities usually realize little revenue relative to the organization’s overall budget and traditional fundraising contributions.” (2004, p. 10).

#### *The Hybrid Spectrum Summarized*

Kim Alter defines a Hybrid Organization similar to how others define “social enterprise”. Her definition of social enterprise is very similar to Muhammad Yunus’ definition of “social business”. She also introduces three different versions of what she calls the social enterprise. With the hybrid spectrum, she adds clarity to the discussion of different organizational models, and this spectrum will be further developed in the next chapter – to clarify and distinguish even more between different organizational models (and sectors).

#### **5.1.2 Existing definitions of the fourth sector**

The next couple of pages will look at some existing definitions of the fourth sector. It is well worth to notice that all of these definitions describe the fourth sector as hybrid companies with a dual purpose of financial and social value creation. In other words, neither of these definitions really adds anything new.

In her article on the front page of the business section of New York Times (May 6, 2007), Stefanie Strom writes about the Fourth Sector, as one of the first serious media outlets to describe the phenomenon. She defines the fourth sector in the following way:

*“The term “fourth sector” derives from the fact that participants are creating hybrid organizations distinct from those operating in the government, business and nonprofit sectors. But because the types of participants vary widely and much of the activity is nascent, no single name for what is occurring has gained broad use.”* (Strom, 2007)

Chris Rabb in Fast Company Magazine comments on Strom’s article online, and describes the fourth sector at the same time:

*“Well, if there are the public, private and non-profit (or "independent") sectors, then this new breed of socially responsible hybrid entities makes up the fourth sector. The fourth sector apparently is what I have previously alluded to as "social enterprises" or what Stefanie Strom's article about the Fourth Sector has also referred to as "for-benefit" companies. (Clearly, a marketing guru didn't come up with that moniker)” (Rabb, 2008).*

One of the institutions to coin the term was the Kaospilot-School in Denmark and their principal Uffe Elbæk. In an article on their website, they define the Fourth Sector as “a sector populated by organizations, institutions and companies that that are characterized by being self-financing – i.e. they operate on the free market, but who, on top of the bottom line, want to be measured and judged on the level of their social, ethical and environmental sense of responsibility” (Kaospilot School, 2005). Elbæk also criticizes fourth sector companies for being terrible at making money and being run by a bunch of idealists that are not really business-savvy.

Uffe Elbæk defines the fourth sector by the following three characteristics (Elbæk, 2004):

1. Financially sustainable organizations, similar to the private sector
2. Social ambition, where the profits benefit a public good
3. Highly motivated and committed employees similar to the nonprofit sector

Another mentionable organization that has been trying to define the field up until now is the Fourth Sector Network ([www.fourthsector.net](http://www.fourthsector.net)). On their website, they describe the fourth sector as follows: “Pioneering organizations in the three sectors are in fact converging toward a fundamentally new organizational sector that integrates social purposes with business methods: a Fourth Sector. In addition to convergence, a second significant pattern of organizational activity has been occurring. The past few decades have seen a proliferation of new hybrid organizational models (Figure 10 below) .....they share two common characteristics - pursuit of social and environmental aims and the use of business methods - that position them within the landscape of the emerging Fourth Sector” (Fourth Sector Network, 1998).

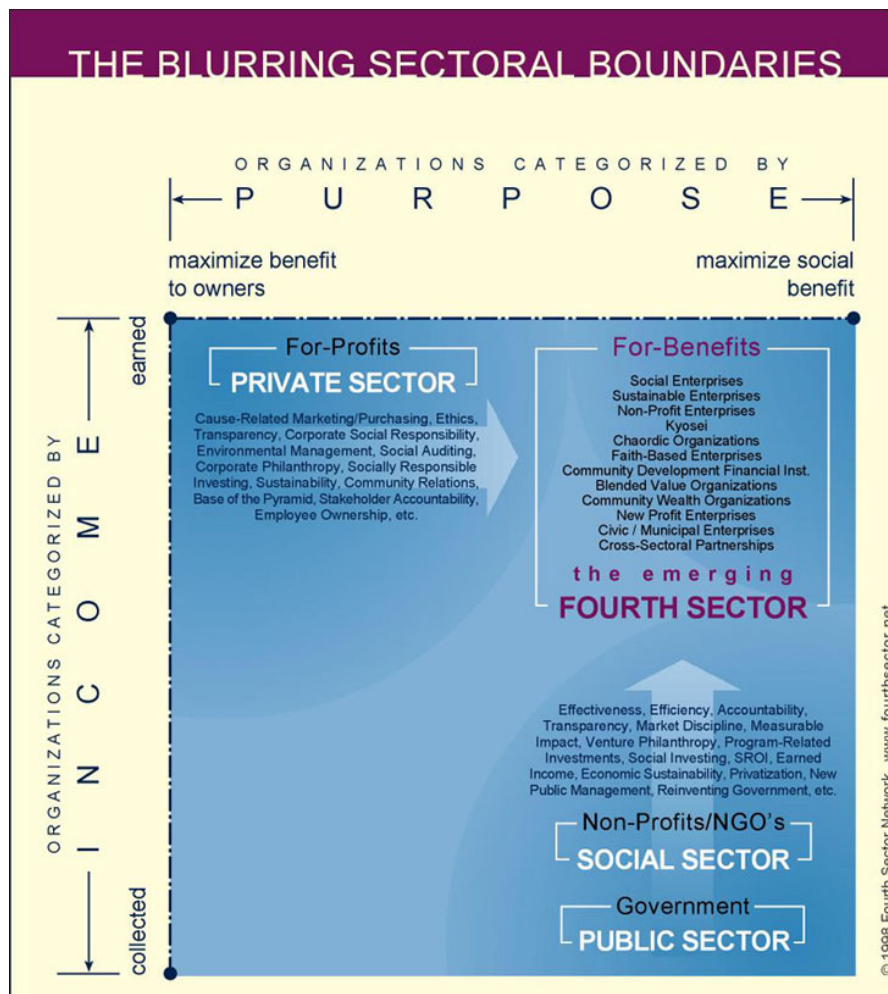


Figure 10 - The Blurring Sectoral Boundaries (Fourth Sector Network, 1998)

# Chapter 6 – A New Definition of the Fourth Sector

The intention of this chapter is to criticize the most relevant definitions from chapter 3, 4 and 5 and then clean up the field of hybrid organizations and the so-called “blurring sectoral boundaries” with a new definition of the Fourth Sector. This definition will make it possible to precisely determine whether an organization is a fourth sector-organization, a social sector organization or a private sector organization. By redefining the fourth sector, the grey-zones in the field of dual value creation will also become more black and white (or perhaps colorful).

The reason why criticism of terms from previous chapters is relevant here is because it will help to contrast the new definition of the fourth sector against weaknesses in other similar definitions.

## 6.1 Criticism of definitions in chapters 3, 4 and 5

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### 6.1.1 Corporate Social Responsibility, CRM and the Triple Bottom Line

Corporate social responsibility, cause related marketing and the triple bottom line all promise more than they deliver. The actual impact measured as a percentage of revenue from these companies is rarely more than a couple percent, and the mission of private companies is still to maximize profits for their shareholders. There are definitely social win-win-win situations to be created, as described by Porter and Kramer in “Strategy and Society”, but this is still nothing but enlightened self-interest. Strategic CSR doesn’t really change the main purpose of a private company, except from realizing that a private company also can benefit society directly through its core offering and make a profit on it at the same time.

That companies practice fair-trade and try to harm the environment as little as possible, is not really more than what one should expect (like when Starbucks brags about paying fair prices to their suppliers and trying to reduce waste by introducing cups made of more recycled materials). This is not “above and beyond”, this is a bare minimum of trying to avoid harming

people and the planet. Starbucks still exist to benefit their shareholders, and they have realized that by not harming people and the planet on the way is an even better way of benefiting their shareholders in the long-term perspective (it is also a risk-mitigation strategy).

Though, there are a handful of companies out there that takes it a step further. Novo Nordisk, the Grieg Group and the Carlsberg Group (as mentioned in 5.2.1) are owned respectively 25.5%, 25% and 30.3% by their purely altruistic foundations, giving away millions of dollars to good causes every year. These are examples of companies that **really** combine a social purpose of their ownership into the business, where the business partially exists to benefit a greater good.

### 6.1.2 Social Entrepreneurship and Social Business

The major issue with Social Entrepreneurship is that it could be anything and everything. If we for example take a look at Reis' definition from Table 4, we can see that his definition is that *“social entrepreneurs create social value through innovation and leveraging financial resources...for social, economic and community development”*. If this definition was the common definition for what a social entrepreneur is, then everything from a private company entrepreneur to a founder of a nonprofit could be a social entrepreneur. Most private companies also create social value through innovation (just look at Apple, Google, Facebook, Microsoft, Pfizer etc), and they help with social, economic and community development – directly and indirectly. A definition that doesn't limit the interpretation of organizations within it in a specific way is NOT a good definition.

Most definitions of Social enterprise usually have something about both social value creation and using business means to achieve this in them, but the definitions rarely state exactly how to distinguish between different types of organizations (private sector, social sector, social enterprise).

Social business at least brings the field to the next level – by categorizing different types of social entrepreneurs/enterprising nonprofits, and classifying social businesses as organizations with nonprofit missions, but with full-cost recovery or more than full-cost

recovery of their operations. The main critique of the term social business is that it applies only to the nonprofit axis (from when an organization moves from a nonprofit towards a social business with more than full cost recovery). It does not explore at all the private sector axis – when a private sector company moves towards becoming a social business. This axis still stands unexplored (or is defined as a dichotomy of either 100% private or 100% social).

### 6.1.3 Hybrid Organizations and the “blurring sectoral boundaries”

The definitions in chapter 5 are not really any different from many of the definitions of social entrepreneurship and social business from chapter 4. In fact, they don’t really look into what a “maximization of social benefit” implies, and there is no clear definition in Figure 10 - The Blurring Sectoral Boundaries (Fourth Sector Network, 1998) for exactly when an organization has enough of a social purpose to go from being a private sector company to qualifying as a fourth sector company (or it seems like it is either 100% for-profit or 100% social purpose – quite black and white). Neither is it clear in Figure 10 how much income a nonprofit needs to have before it becomes a fourth sector organization. The figure might be called “blurring sectoral boundaries” for a reason, namely that the field still is blurry, and with these definitions it is impossible to determine exactly *what sector an organization belongs in*. **This is a major weakness.**

In other words, the critique towards the term of social entrepreneurship for being too widely defined also applies to the current definitions of the fourth sector. It seems like the definitions of the fourth sector above are more closely aligned to Muhammad Yunus’ “social business enterprise” and what Kim Alter defines as a social enterprise in her paper “a social enterprise typology” - “*any business venture created for a social purpose – mitigating/reducing a social problem or a market failure – and to generate social value while operating with the financial discipline, innovation and determination of a private sector business.*” (2004, p. 11)

Neither Muhammad Yunus nor Kim Alter defines clearly the private sector axis for when a private company turns into a social business or a social enterprise, and Yunus includes full cost recovery nonprofits in his definition of social business. Alter also distinguishes between “nonprofit with income-generating activities” and “social enterprise”, where the transition



happens at full cost recovery. Both these definitions are on the nonprofit axis – moving from a traditional nonprofit to a social business (Yunus) or a social enterprise (Alter).

The author wants to take these definitions a step further and discuss whether a full-cost recovery organization is really financially sustainable in the long term, and also introduce an addition to the “private sector axis / - continuum” of organizations transitioning from the private sector to the fourth sector. This continuum has up until now not been defined with a clear divide between private sector and the fourth sector, making it difficult to operationalize and categorize different types of businesses.

The addition that will be made to this continuum is businesses where at least 50% of the purpose is to benefit a greater, public good, proven by giving away 50-99% of their profits or dividends (or owned at least 50% by a purely altruistic owner) – an organizational model that has not been mentioned in descriptions of neither corporate social responsibility, social enterprise, social business, hybrid organizations nor existing descriptions of the fourth sector.

## 6.2 Defining the Fourth Sector

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There are some important prerequisites that apply to fourth sector companies:

1. Fourth Sector companies need to maximize their long-term profits to be able to compete on equal terms with private sector companies. This implies more than just full cost recovery. This implies maximizing revenue and minimizing cost. A Fourth Sector company needs to benchmark towards the leading companies in the industry it is operating in (on leadership, innovation, quality, efficiency etc). This does **not** mean that a Fourth Sector Company cannot run with deficit for a year or three and thereby be disqualified from the fourth sector, but the long-term objective needs to be profit maximizing to be able to compete with the private sector.
2. Long-term financial sustainability is essential, like in the private sector, to ensure long-term growth of the organization. This implies responsible financial management with a growth focus (more than a year-over-year perspective)

3. A natural consequence of responsible financial management is the separation of business costs and social program costs. To be able to maximize revenue and minimize unnecessary costs, a Fourth Sector company needs to avoid having expenses that are not in the organizations' long-term financial self-interest.
4. A Fourth Sector Company has institutionalized altruism. 50-100% of end year dividend (or 50-100% of profit that is possible to give away without compromising long-term growth) from a Fourth Sector Company is given away to benefit a greater, public good – locally or globally. The reason for why the division is at exactly 50% is the simple fact that it makes the company half-and-half – a true hybrid between private/social purpose, and therefore also a Fourth Sector Company. Anything less than half, and it is a private sector company.
5. Fourth Sector companies do not harm people and the planet – they do not behave unethically. Even hardcore supporters of the Friedman shareholder focus within the CSR-debate agree that harming people and the planet is unsustainable in the long run, e.g. it will hurt a company's profit maximization over time if the company is behaving unethically/exploiting people and the planet.
6. The classical Friedman-Freeman debate is irrelevant for the coming definition of the fourth sector.

Based on these prerequisites I will propose to define a Fourth Sector Company (or a greater good corporation) as follows:

*“A Fourth Sector Company is a long-term financially sustainable organization, whose purpose is at least 50% to benefit a greater, public good. The organization redistributes its creation of wealth directly towards a greater good by philanthropically giving away 50-100% of its dividend (alternatively 50-100% of profit possible to give away without compromising long-term growth).*

An immediate implication from this definition is that one of governance or ownership of a Fourth Sector Company (FSC). Since at least 50% of dividends should benefit the greater

good, the FSC needs to find a sustainable solution for how this can be incorporated into the legal governing framework of the organization and overseen in the interest of the cause(s) the FSC is meant to benefit. Transferring 50% or more of the ownership (shares) to a foundation or a legal entity with a purely altruistic motive can be one solution.

Again, the reason for why the purpose needs to be at least 50% to benefit a greater, public good is that at 50 percent the company is exactly half-and-half (and a true hybrid between 50% private company and 50% social purpose). This is the minimum of what can be expected from a fourth sector company. If 49% of the purpose is to benefit the greater good, it implies that 51% of the purpose is to benefit the private shareholders, something that makes it more of a private company than a social purpose business (and this is NOT a fourth sector company). It is a socially responsible business. The Grieg Group is for example 25% owned by the altruistic Grieg Foundation (something that makes it an exceptionally socially oriented private sector business) whereas the apparel company Me to We Style Inc gives away 50% of its net profits to a children's charity and is therefore a fourth sector company (barely).

The archetypical Fourth Sector Company:

- Gives away 100% of its dividends (or is 100% owned by a owner with a pure altruistic motive with the ownership)
- Has got a long-term objective of profit maximization, but with stakeholder focus and strategic CSR
- Is not harming people and the planet
- Is transparent and trustworthy
- Is benchmarking itself against the leading private company in its industry

There are more immediate questions and implications arising from the definition above that will be discussed later in this chapter, but first the definition will be explained below in Figure 11 - The Fourth Sector Matrix, in order to visualize some of the key elements of the definition and its prerequisites. Then the author will present a revised version of Kim Alter's Hybrid Spectrum from Chapter 4, based on the author's review and definition of existing and new organizational models.

## 6.2.1 The Fourth Sector Matrix

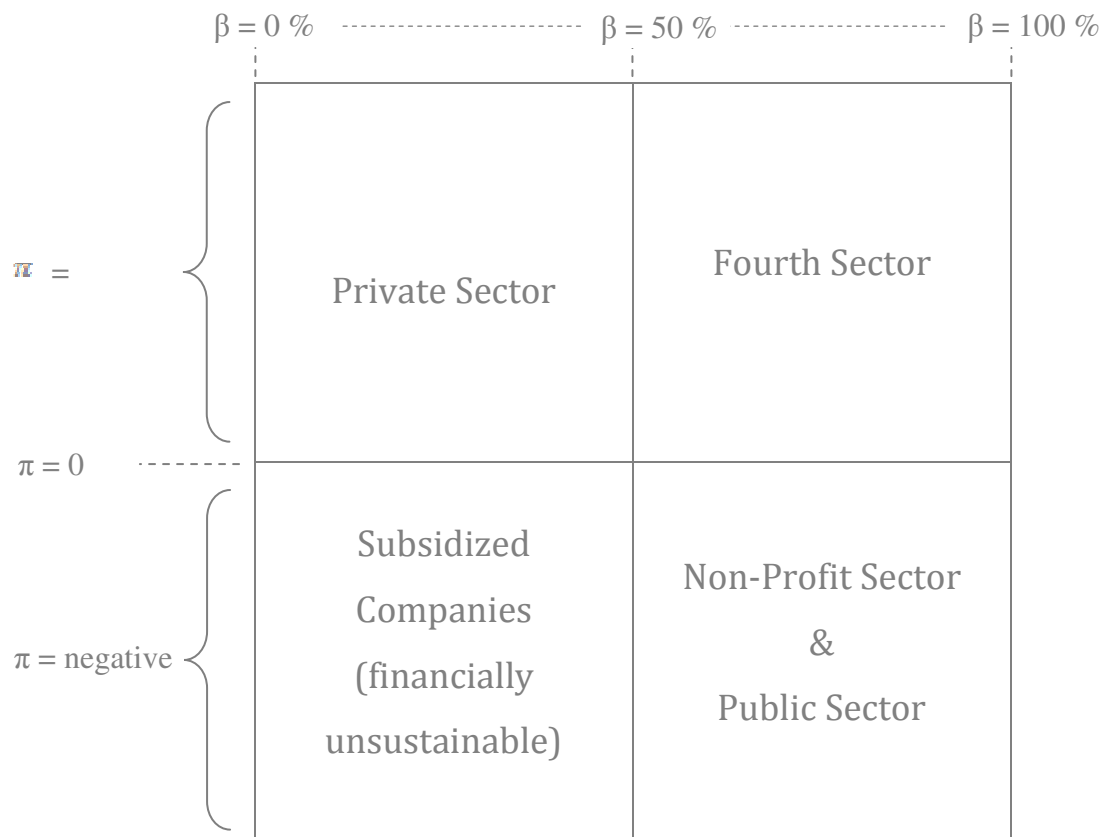


Figure 11 - The Fourth Sector Matrix

- $\beta$  = how much of business purpose is to benefit a greater, public good
- At  $\beta = 50 \%$ , half of dividends are given away towards a greater good
- At  $\beta = 100 \%$ , all of dividends are given away towards a greater good
- At  $\beta = 0 \%$ , dividends are paid out to shareholders 0 to a greater good
- A model where it is donated from net profits or revenue can be considered as a Fourth Sector-model, if what is given away is equal to or greater than dividends paid out to shareholders. Though, this is not recommended since it could potentially compromise long-term sustainable growth of the organization
- $\pi = R - C$  where [  $R$  = revenue ] and [  $C$  = cost ]

## 6.2.2 The Sector Continuum

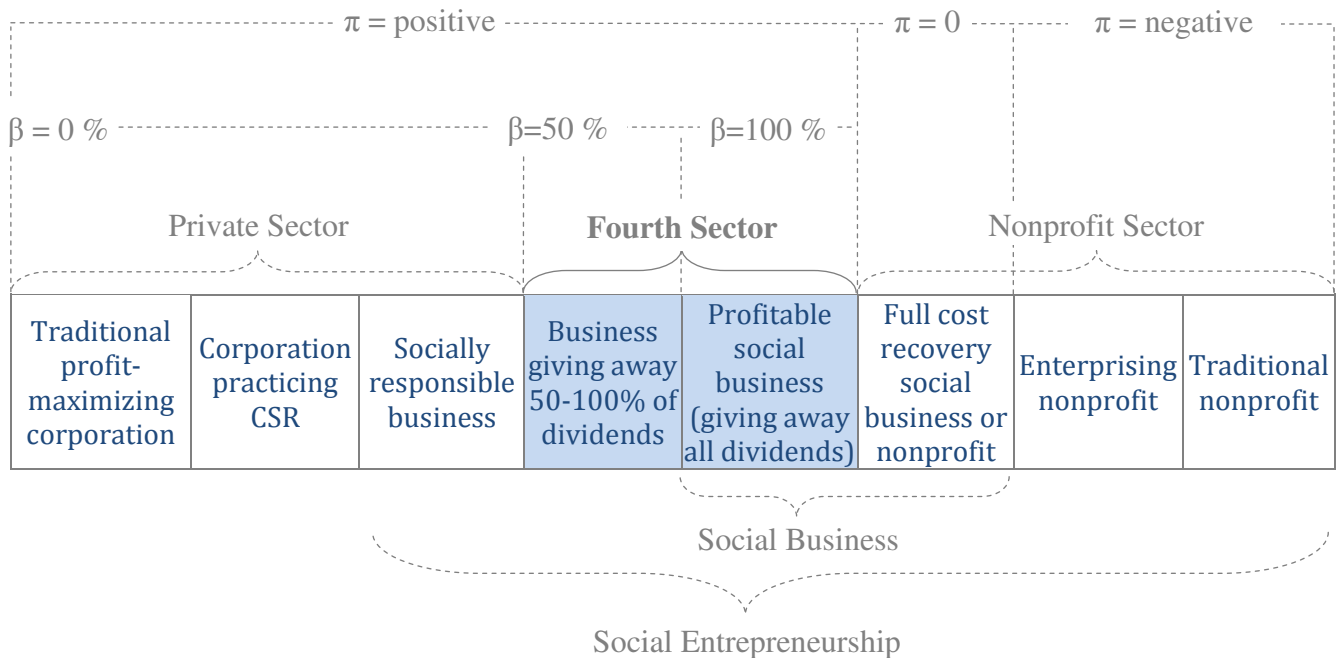


Figure 12 - The Sector Continuum

## 6.3 Clarifications

### 6.3.1 Revenue vs. Dividend / Profit / Ownership

Some FSCs would prefer to give away a high percentage of sales or revenue directly to good causes, to have an immediate impact. To qualify as a FSC if you give away directly from your revenue, then what is given away on an *annual basis* needs to be equal to or larger than what shareholders are paid out in dividend.

One of the most obvious problems of promising customers to give away a certain amount directly from revenues/sales, is that the financial control most likely will decrease and the risk of not being profitable increases. The motto here is: don't give something away until you know what you actually have available to give away.

Long-term growth of the company is very important to ensure a maximization of social sustainability and capital available to give away. An FSC should not donate money to good causes if it compromises the organization's long-term survival (something that would be both financially and socially unsustainable and not beneficial for anyone). This is the reason why it is suggested that a FSC gives away 50-100% of its *dividends*, because then the capital need for sustainable organizational growth will already have been discussed, and what is given away will not compromise the growth of the organization. If the same financially responsible mentality is applied if 50-100% of profits are given away, then there is nothing wrong with that (and the company is definitely a true FSC).

Another relevant situation that will classify as a FSC is when there is 50% or more ownership (of the shares of the FSC) by a purely altruistic owner, which wants to benefit a greater, public good with the ownership. This owner could be a foundation (the Kavli Foundation owns 100% of the Kavli Group in Norway, getting 100% of the dividends payable. The Kavli Foundation gives away millions of Norwegian Kroner every year to a variety of good causes locally and has been benefiting society for years) or the owner could even be the government of a country. The government is an owner with a social purpose of its ownership – i.e. to benefit the people of its country, which definitely can be classified as a greater, public good. This is like an enormous co-operative, where all citizens of a country have a stake in the corporation. By opening up for public ownership as a part of the social purpose behind a company has got interesting consequences – given the definition and cut-off point of 50%. A direct implication is that the fourth sector is way bigger than expected, because partial government-owned companies can be classified as FSCs, since they basically help to benefit a public good (dividend goes to the government, also known as the people of the country in scope). In other words – companies like StatoilHydro, Telenor, TeliaSonera and Scandinavian Airlines can all be classified as Fourth Sector Companies, as they have 50% or more ownership by various governments in Scandinavia, and basically exist partially to benefit the public greater good.

## 6.4 What is not a Fourth Sector Company?

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A for-profit business with a great social impact through its core product offering is not a FSC unless the purpose of the company's existence is at least 50% to benefit the public good, proven by giving away at least 50% of its dividend (or profits) to a greater good cause. A for-profit business can have a greater social impact than a FSC (and than a nonprofit) without being classified as a FSC, even with a model of shareholder profit maximization. An example of this could be a privately held for-profit company selling cheap solar panels to unpowered villages in developing countries, radically altering the lives of thousands of people (a great social impact), but turning a profit at the same time, creating win-win situations.

A full-cost recovery (but not profitable) social business is not a FSC, since it is spending on social programs directly in its value chain (most likely not financially efficient, and it will be difficult to compete with private sector companies). In a cost-recovery mode, the objective is to have zero profit, e.g. the social business will spend money on irrelevant expenditure, seen from a business perspective. Profit maximization does not give any incentives to give away money to social programs if you don't get a return on investment (in a long-term perspective). Private Sector acts ethically to make money; FSC makes money to act ethically.

An example of an inefficient full-cost recovery could be a nonprofit hospital that makes enough revenue to offset its own cost. If the entity starts to directly subsidize prices of their services (because they are not required to make a profit and can reinvest the revenue directly back into operations) with let's say 10%, this subsidy can eventually back-fire. If their privately held competitor realizes that their prices also needs to come down 10% to be able to compete with the nonprofit entity, they might find ways of reducing their cost (such as implementing a new IT-system that reduces (manual) labor costs and results in a 10% overall savings), where the nonprofit entity would still have the higher manual labor cost (because they didn't need to innovate/rationalize due to the artificial cost subsidy) and thereby lose their competitive edge over time due to their nonprofit full-cost recovery only-business model. The long-term objective of FSCs therefore needs to be profit maximization, to be able to fully compete with – and be a serious alternative to their private sector competitors.

## 6.5 Examples of Fourth Sector Companies

Company Name	Industry	Fourth Sector Classification	Website
Me to We Style	Apparel	50% of profits to charity	<a href="http://www.metowestyle.com">www.metowestyle.com</a>
God El	Power	100% owned by own foundation	<a href="http://www.godel.se">www.godel.se</a>
Hives for Lives	Honey	100% of profits to charity	<a href="http://www.hivesforlives.com">www.hivesforlives.com</a>
Give Something Back	Office Supplies	More than 50% of profits to local communities	<a href="http://www.givesomethingback.com">www.givesomethingback.com</a>
Newman's Own	Food	100% of profits to charity	<a href="http://www.newmansown.com">www.newmansown.com</a>
Live	Energy Drink	50% of profits from every purchase to charity	<a href="http://www.drinklive.org">www.drinklive.org</a>
Athena Water	Water	100% of profits to charity	<a href="http://www.athenapartners.org">www.athenapartners.org</a>
Belu	Water	100% of profits to charity	<a href="http://www.belu.org">www.belu.org</a>
One	Water & Condoms	100% of profits to own charitable foundation	<a href="http://www.onedifference.org">www.onedifference.org</a>
Kavli Group	Food	100% owned by the Kavli Trust	<a href="http://www.kavli.com">www.kavli.com</a>
Scandinavian Airlines	Airline	50% owned by Sweden, Norway and Denmark	<a href="http://www.flysas.com">www.flysas.com</a>
TeliaSonera	Telecom	51% owned by Sweden and Finland	<a href="http://www.teliasonera.com">www.teliasonera.com</a>
Telenor	Telecom	53.97% owned by Norway	<a href="http://www.telenor.com">www.telenor.com</a>
Kongsberg Group	Technology	50% owned by Norway	<a href="http://www.kongsberg.com">www.kongsberg.com</a>
StatoilHydro	Energy	67% owned by Norway	<a href="http://www.statoilhydro.com">www.statoilhydro.com</a>

Table 6 - Examples of Fourth Sector Companies



## 6.6 Criticism & Issues

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*“While many signs point toward the emergence of a Fourth Sector, a fully developed supportive ecosystem for Fourth Sector enterprises (legal structures, capital markets, technical assistance, etc.) is not yet in place”* (Fourth Sector Network, 2007)

- One of the biggest criticisms of the FSC is also its social advantage – the fact that 50-100% is given away. This means that you have 50-100% less shares to play with, or that shareholders will only get 0-50% of the dividends. The implications can be grave when a FSC needs to raise capital, either for survival or expansion – and a whole new financial system needs to be created to support the sector. The Sector is still too young to really predict what will happen in situations like these, even though there are indications that there is a market for “social capital” (less financial but more social return, in line with the more complex motivations of *homo oeconomicus maturus* from chapter 2). Many emerging micro-credit institutions is a sign of exactly that – people are willing to lend money (without making a profit) to organizations and people with a social purpose/focus on benefiting the greater good. There is a great social impact, and the “donors” get their money paid back over time (often with interest), something that cannot be said for purely philanthropic contributions to a nonprofit. Muhammad Yunus predicts that there will be capital available for this part of capitalism as well, but this might turn out to be the biggest weakness of the fourth sector.
- Competing on same terms as the private sector could be a challenge for FSCs, especially if the financial compensation tools (options, shares, dividends etc) of the private sector cannot be replicated into the fourth sector. But then again, if the theory of the modern economic man and expanded motivations is right, human beings are more complex and wants more from life than just maximizing their financial situation, and the new, postmaterialistic utility curve of human choice might give us some interesting surprises.
- How does a FSC determine what a good social purpose is? What greater good should it benefit, and how does it know that this is a *good* greater good to give money towards? This will probably be adjusted over time, since most FSC compete in the

capitalistic marketplace, and the market will probably determine whether the cause(s) the FSC supports are good enough. If the market doesn't like the cause(s), it will probably be more hesitant to support the FSC as well.

- What is the actual social impact of a FSC compared to a nonprofit or a private company? This is a very valid question, and there is not a straightforward answer. A private company might even have a greater social impact than both a FSC and a nonprofit. If the organization (private, public, fourth or nonprofit sector) is set up to have the greatest possible social impact through all of its operations and it is clearly measured and reported what the actual social impact is; that will probably be the best way to benefit a greater good, regardless of sector.
- One can claim that the reputation of a FSC is more at risk than the reputation of a less socially purposeful company. The more you claim to do good, the higher your pedestal rises (and the harder the downfall gets). This is a valid claim that also applies for socially responsible companies. The solution is to be transparent, communicate what you actually do and not overpromise (Swaen & Vanhamme, 2004).
- If a private company owned 50% or more by a government (plus state, county and municipality) is a FSC, then what about other forms of Institutional Ownership? Can Pension Funds controlled by governments be classified as ownership for the greater good? What about pension funds or funds controlled by special interest groups, such as Teacher's Union or religious groups? One can claim that if there are special (private) interests behind the ownership, then this is not to the benefit of the greater, public good, and it is not fourth sector, but private sector.
- Can the fourth sector model be seen as an additional, voluntarily paid tax? Yes, definitely. An essential point about fourth sector companies is that they are trying to ensure a more direct, more efficient redistribution of wealth towards those in need (more than the current indirect version of capitalism and governments). Tax level in the country of operation is irrelevant, since 50-100% of dividends (or gross/net profits) given away is still 50-100% of what is available to give away (50-100% of the purpose is to benefit a greater, public good). Whether what you give away is before or after tax does not matter in principle (even though the actual amount could become different in practice, due to different tax levels and tax laws in different countries).

## 6.7 Chapter Conclusion

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There are issues with the current version of capitalism. Historically, there has been too much shareholder greed, and profits have been maximized at the cost of exploiting people and the planet. People usually don't know shareholders' ethics and motives behind their ownership, and because of negative historical incidents they tend to assume that the standard shareholder motive is greed and profit-maximization. With the financial meltdown in Q4 2008 and Q1 2009, more people than ever are asking for a more human face to capitalism.

The Fourth Sector Company is one such alternative - a solution that can be found in the use of market mechanisms and the capitalistic system, in the real spirit of Adam Smith. The major difference from the old version of capitalism is in the motives of ownership and governance, ensuring a more direct and efficient redistribution of wealth towards those in need in our world than towards profit-hungry shareholders motivated by personal greed.

The genius of capitalism is thereby unleashed to advance the public good, and Greed turns out to be really good - when it comes to helping others. This is the promise of the Fourth Sector Company.

The idea of the Greater Good Corporation itself is not novel. But the new momentum this idea has gained in society is notable, something that leads to an entirely new emerging sector.

The fourth sector company deserves its own definition, clearly distinguished from the fields of social enterprise and social business, CSR and hybrid organizations. In this chapter, this definition has been presented and will hopefully help to operationalize different business models, and clarify the different types of organizations with dual social and financial value creation and what really separates them. It is most likely one the first definition of its kind that describes companies where 50-99% of the purpose is to benefit a greater good (and the other remaining 1-50% is to benefit the shareholders) – with some radical consequences such as having partially government own businesses classified as FSCs.

The fourth sector is above and beyond the field of Corporate Social Responsibility and enlightened self-interest, and free from the classical Friedman-Freeman debate. It is institutionalized altruism and philanthropy.

The definition presented above has guaranteed got some good potential for improvement, and there are questions that still need to be answered (such as the potential lack of access to capital for fourth sector companies?). Some of these questions need to be dealt with on a more systemic level, but nothing is better than actually getting the debate started. This definition of the fourth sector will hopefully help to clarify the field that is being discussed, by making it more tangible and more crisply defined. And with a more tangible definition it is also easier to make tangible additions to the definition (plus more tangible counter-arguments) and going forward more tangible solutions will inevitably arise.

## Chapter 7 – Theoretical Framework for Strategic Analysis: A Resource-Based View

The next two chapters intend to analyze whether two fourth sector companies, God El and Me to We Style, might have competitive advantages or disadvantages as a consequence of their fourth sector business model (and how this is aligned to trends in society, through looking at some relevant surveys). This will be done by conducting an internal analysis of the companies in order to find resources and capabilities that translate into strengths and weaknesses in the respective organizations and their business models.

An external analysis of the industry the companies operate in will not be relevant here, since the intention is to look at differences in competitiveness due to the fourth sector business model exclusively. This is an internal firm-specific difference and therefore not relevant to the industry as a whole (the industry is the same for all the players in that industry).

All other elements than those affected by the fourth sector business model will be held equal and isolated from this analysis – assuming that a private sector company and a fourth sector company in theory can perform equally well since they are both profit maximizing entities within a free market system. In the real life, all companies will of course perform differently due to multiple reasons. But because it is suitable in this dissertation, everything except from the business model and the consequences it brings along will be seen upon as irrelevant for the discussion of the competitiveness analysis

### 7.1 Defining Competitive Advantage

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A company is said to have a **competitive advantage** over its rivals when its profitability is greater than the average profitability for all firms in its industry. The greater the extent to which a company's profitability exceeds the average profitability for its industry, the greater is its competitive advantage. A company is said to have a **sustained competitive advantage** when it is able to maintain above-average profitability for a number of years (Hill & Jones, 2004, p. 4).

If competitive advantage is achieved, then superior profitability will follow. Therefore, the primary objective of *strategy* is to achieve competitive advantage. At the most basic level, how profitable a company becomes depends on three factors (ibid):

- 1) The amount of value customers place on the company's products
- 2) The price that a company charges for its products
- 3) The costs of creating that value

To achieve competitive advantage, a company must create **distinctive competencies**. These are strengths specific to the firm that allows it to *differentiate* its product and/or achieve *lower cost* than its rivals through its activities - through having superior *efficiency, innovation, quality, and customer responsiveness*.<sup>6</sup> Distinctive competencies arise from two complementary sources – **resources** and **capabilities**.

*Resources* can be divided into tangible (physical) and intangible (nonphysical) resources, and are the capital, physical, human, organizational, technological or relational factor endowments that allow a company create value for its customers. If a resource is difficult to imitate and firm specific, it is more likely that this resource leads to a distinctive competency. *Capabilities* refer to how good an organization is at coordinating and putting its resources into value-creating use (structures, systems, routines, processes, interaction, culture, leadership).

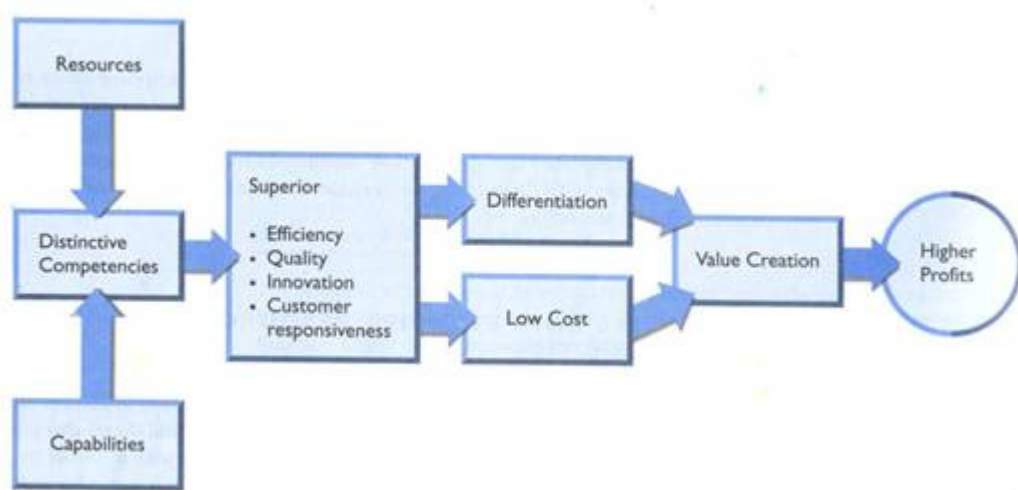


Figure 13 - The roots of competitive advantage (Hill & Jones, 2004)

<sup>6</sup> It is important to remember that a company's profitability is also affected by the characteristics of its industry, and that different industries are characterized by different competitive conditions.

## 7.2 Identifying Competitive Advantages

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To identify and evaluate which competitive advantages the company has, two complementary models are being used, EQIC (Efficiency, Quality, Innovation and Customer Responsiveness) and VRIO (Value, Rarity, Imitability and Organizational). First, the EQIC-model will be used to identify which activities in the company that can create the competitive advantages and which resources and capabilities that makes it possible to perform these activities (this model can also be used in conjunction with Michael Porter's value chain-model. Though, the two models are overlapping and Porter's Value Chain will be left out here). Thereafter the VRIO-analysis will be used to find out if any of the resources or capabilities can make a sustained competitive advantage for the company<sup>7</sup>. Causal ambiguity can often make it difficult to detect what the real value drivers of a company are, even for the managers of the firm. Thus, the use of the VRIO framework is as complex as the nature of the resources (Peng, 2006).

### 7.2.1 The EQIC-model

According to the EQIC-model there are four generic main concepts that can contribute to competitive advantages in relation to other companies. These concepts must be looked at together since they have a mutual affect at the competitive advantages. The four concepts are Efficiency, Innovation, Quality and Customer responsiveness. (Hill & Jones, 2004)

#### **Efficiency**

The company with the highest productivity per invested money and per employed will have the highest efficiency, when everything else is constant. This means; the less inputs needed for the production the better. (ibid)

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<sup>7</sup> It is important that top managers do not make the mistake of overemphasizing current profitability to the detriment of long-term profitability. The overzealous pursuit of current profitability to maximize short-term returns can encourage such misguided managerial actions as cutting expenditures judged to be nonessential in the short run – for instance, expenditures for research and development, marketing and new capital investments. Although cutting current expenditure increases current profitability, the resulting underinvestment, lack of innovation, and diminished marketing can jeopardize long-run profitability. These expenditures are vital if a company is to pursue its long-term mission and sustain its competitive advantage and profitability over time (Hill & Jones, 2004, p. 15).

To guard against short-run behaviour, managers need to ensure that they adopt goals whose attainment will increase the long-run performance and competitiveness of their enterprise. Long-term goals are related to such issues **as product development, customer satisfaction, and employee productivity**, and they emphasize specific objectives or targets concerning such things as efficiency, product quality and innovation (ibid).

## Quality

A higher price on a product can be justified for a customer as long as the quality of the product is better. This is thanks to the different characters of the product that the customer value more than at the competitors similar products. It has been proved that the reliability of a product is one of the most important factors from the customers' perspective. (Hill & Jones, 2004)

## Innovation

Product innovation or processing innovation can give unique products with superior characters. This will lead to differentiation which means that a company can take a higher price for their products. (ibid)

## Customer responsiveness

Customer responsiveness is all about being better than the competitors to identify and live up to the customers' needs and wants. This can be done both by tailor-made products to the customers and by quick and good response to the customers wants. Innovation and quality is a requirement to satisfy the buyer (ibid).

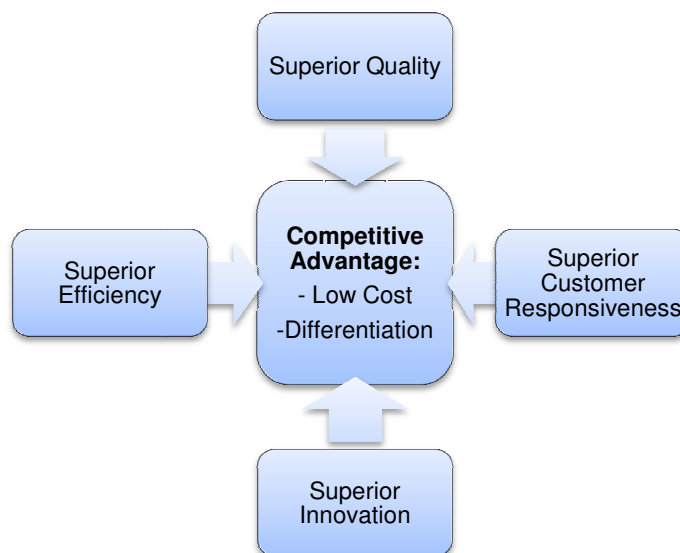


Figure 14 - Generic building blocks of competitive advantage (Hill & Jones, 2004)



### 7.2.2 VRIO-analysis

Company specific resources and capabilities can be the source of sustained competitive advantage. If such strategic resources or capabilities are the source of sustained competitive advantage, they have to be valuable, rare, inimitable, and exploited by the organization. This is known as the VRIO framework (Peng, 2006). There are two key assumptions in the VRIO framework - the assumption of *resource heterogeneity* (every firm has a unique combination of resources and capabilities) and the assumption of *resource immobility* (resources and capabilities unique to one firm cannot easily migrate to competing firms). More specifically, what does it mean that a company has got valuable, rare, inimitable resources or capabilities that are exploited by the organization?

- *Valuable resources and capabilities* - Only value-adding resources can possibly lead to competitive advantage, whereas non-value-adding capabilities may lead to competitive disadvantage. (ibid) Valuable resources or capabilities are essential for the company's ability to compete in the industry,
- *Rare resources and capabilities* - How rare are these valuable resources and capabilities compared to what the competing firms have? The resource is rare if the competitors don't have the same quality or quantity of the resource. Only valuable and rare resources and capabilities have the potential to provide some temporary competitive advantage. (ibid)
- *Costly to imitate the resources or capabilities* - A resource or capability can be imitated both by direct duplication and substitution. If the resources or capabilities of the company are difficult to imitate, a competitive advantage is more likely. Intangible resources are extremely challenging to imitate, whereas tangible resources easily can be imitated. Valuable, rare and inimitable resources can potentially lead to a sustained competitive advantage. (ibid)
- *Resources and capabilities are exploited by the organization* - To realize a potential sustained competitive advantage, the company will have to organize in a best possible way to develop and leverage the full potential of its resources and

capabilities (ibid). The company should use the resource to create value, the resource should fit to the company, and the value that is created should be kept within the company. (Jakobsen & Lien, 2001)

The EQIC-model serves as a basis for the VRIO-analysis and helps to identify which resources and capabilities that might be especially important for the company subject to the analysis.

<b>VRIO Criteria</b>	<b>Explanation</b>
<b>Valuable</b>	Is this resource/capability a primary source of product value for the firm?
<b>Rare</b>	Does the activity include a resource or capability controlled by the firm and rarely available to competing firms?
<b>Inimitable</b>	Do competing firms have a cost disadvantage when imitating the scarce resource or capability held by the new venture firm?
<b>Organizable</b>	Is the activity critical to the mission of the firm, and is the firm organized to exploit this valuable, rare, and costly-to-imitate resource or capability?

**Table 7 - The VRIO-criteria**

## Chapter 8 – Empirical Data & Analysis

This chapter will present two fourth sector company cases (Me to We Style and God El), analyze whether they might have competitive advantages/disadvantages because of their fourth sector business model, and look into how this is aligned to trends in society, described in some relevant surveys. The God El-case is based on information available on God El's homepage (God El, 2009) and on an interview with God El-Founder Stefan Krook (appendix 4). The Me to We Style case is based on the author's position as Director of Strategy and Business Development with the enterprise from August 2007 to July 2009.

### 8.1 Case Presentation

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#### 8.1.1 Me to We Style

Me to We Style Inc is a Toronto-based apparel company, founded December 2005, selling since April 2007. They provide basic, high-quality apparel to socially responsible consumers, organizations and corporations, and all their clothing is made with eco-friendly, organic fabrics and without sweatshop labor. The manufacturing takes place in Canada, and Me to We Style is the first North-American apparel company to go through a full social audit in their supply chain by the International Fairtrade Labelling Organization (FLO). Me to We Style sells both retail products to end-consumers and custom printed wholesale products to companies, universities, NGOs, events, bands, teams and organizations.

Me to We Style has chosen a business model where they have entered a full partnership with a charity called Free The Children. 50% of profits (pre tax, end-year) are donated directly to Free The Children, in order to create a long-term revenue stream for the charity (which makes the charity less sensitive to volatility in the market for philanthropic contributions). Free The Children is a children's charity that was founded in 1995 to fight child labor through education, and is now the world's largest network of children helping children through education. The other 50% of the profits in Me to We Style is reinvested into the enterprise to ensure profitable growth. Me to We Style is managed on profit maximization principles, competing head-on with private companies in the apparel industry.

In the two first years with revenue, Me to We Style has been able to contribute more than \$150,000 CAD towards Free The Children, both through profits and by setting up other strategic alliances that have generated donations to the charity.

In January 2009, Me to We Style went through its first capital expansion, when Jeff Skoll's Participant Media took a 10% ownership stake in the enterprise. Me to We Style was founded with a very modest equity-base, and has been growing organically under a bootstrap-financing venture-model. By the end of the second year selling, Me to We Style had revenue of around \$1.4 million CAD.

Me to We Style has chosen a differentiation-strategy, where the products are priced 10-30% higher than the average in the industry. There is a strong focus on product quality and intangible product values, through the eco-friendly fabrics, the fair trade manufacturing and the fourth sector business model where 50% of profits are donated to Free The Children.

### 8.1.2 God El

God El is a Swedish power-company founded in 2005, alongside with their holding company GoodCause Holding (100%) ownership, and the GoodCause Foundation (100% ownership of GoodCause Holding).

God El provides cheap power to Swedish households, and gives away 100% of dividends to good causes, such as SOS Children's Villages, Save The Children, Stockholms Stadsmission, Doctors without Borders and Naturskyddforeningen. The customers can help influence which charity their part of the profits shall be given to.

God El was founded with a donation of 11million SEK from several stakeholders, and with a no-interest loan from the company Catella. In addition, Catella provides loans as a security that God El needs to be able to trade on the Northern-European power-exchange NordPool.

God El's fiscal year ending May 2007 was the first profitable year for God El – and 500,000 SEK was given away to good causes. In 2008, 2,2 million SEK was donated, and for the fiscal year ending May 2009 this grew to 3,5 million SEK.. God El follows a low-cost

strategy (combined with simplicity, transparency and honesty), and wants to be able to provide the cheapest product in the market. Management compensation is lower than market, and the executive board receives no compensation. God El has got 80,000 customers (of a total market of 1,5 million in Sweden), and is the fastest growing power-company in Sweden. Their break-even is at 25,000 customers.

## 8.2 EQIC-analysis

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A prerequisite for potentially having a competitive advantage as a consequence of having a fourth sector business model (where the purpose is 50-100 % to benefit a greater, public good), is that the greater good-purpose has to be communicated externally and internally to all stakeholders. Only 5% of the Kavli Group's customers know that they give away 100% of their profits to good causes every year (appendix 4). Their greater good purpose is in other words heavily under-communicated to their customers, and as a consequence they cannot expect any enhancements in customer-brand relations due to their fourth sector business model.

### 8.2.1 Me to We Style

- *Efficiency*

Due to the business model, Me to We Style is able to attract highly qualified labor at a lower-than market cost, plus a volunteer workforce of around 20 volunteers. Several people are willing to work for the company compensated on performance only. In addition, Me to We Style has been able to get free consulting services, free newspaper advertisements, other advertisements at 95% of original cost, conference and tradeshow attendance at 50-100% of original cost, substantial discounts from a range of suppliers, highly discounted cellphone-plans, highly discounted hotel-rates, 70%-90% off on expensive CRM and ERP-software, plus preferred status with several suppliers and distributors – implying beneficial payment terms. Me to We Style has been given free professional fashion photography, photoshopping services and models, and graphic design services and multimedia has been free or at lower-than-market rates.

There is a strong companywide commitment to efficiency, and always asking for preferred rates as a consequence of the greater good purpose of the company. Because of the commitment to efficiency, Me to We Style was able to turn a profit the second year selling, something that is very unlikely in the apparel industry due to heavy investments in fabrics and stocked items.

- *Quality*

N.A The quality of products from Me to We Style is equal/better than those of competitors. This is not directly related to the business model, and therefore not applicable. The perceived intangible quality of the product as a consequence of the business model, combined with other elements such as quality, eco-friendliness and fairly traded, makes customers want to pay a premium for these products. How much of this that is a consequence of the fourth sector business model, is not possible to predict at this moment – but it would be natural that it is at least 25% of the price difference, given that it is 1 of 4 factors that distinguishes the Me to We Style products. Many customers are more than willing to pay the price, which shows that perceived product *value* might be even higher than the product *price*.

- *Innovation*

N.A, except from the fourth sector business model itself. Everything else is run on equal terms as any competitor in the apparel industry.

- *Customer Responsiveness*

Customer Loyalty for wholesale customers is in general very high – above 85%. There is a strong focus on customer service, customization, response- and delivery times, also because of willingness to stretch further on the supplier side. Because of referrals and telling the story of the business model, Me to We Style has been able to get introductions into a wide range of well-known people and companies within its first two years selling, something that will be highly beneficial for future growth. Some of the most respected corporate customers of Me to We Style include Dell USA, Aveda, Ernst & Young, Interface, MTV, Whole Foods Market, Cervelo Cycles, CBS and Unilever.

There is a great attitude among staff and leadership in Me to We Style, with a strong belief in the greater good mission of the company, something that leads to enhanced commitment and increased overall performance.

### 8.2.2 God El

- *Efficiency*

God El has got the lowest pricing in the industry – selling the electricity at cost to their customers. In addition, a monthly fee of between 29,- to 79,- SEK is charged the customer, depending on their annual use of power. Employees in God El are paid lower than market-wages, and it has been relatively easy to attract high-quality, well-educated labor for God El.

As a consequence of their business model, God El has received free furniture for the office, free legal consultation, free IT-services, free graphical design, and a free commercial on national TV as well.

God El has also been given the possibility to recruit customers inside a major mall (Åhlens) in Stockholm, where no competitors are allowed to sell their services.

- *Quality*

N.A. due to a homogenous product (power/electricity to households)

- *Innovation*

Partially N.A. due to a homogenous product. God El has innovated on the business model, combining a low-cost strategy (providing electricity at cost, plus a small monthly fee to the consumer) with 100% of dividends to good causes. In addition, the customers can participate in choosing which charity that should get their share of the profits.

- *Customer Responsiveness*

In April 2009, God El won the price for best customer service in their industry in Sweden, and even finished second best on customer service in general in the nation.

God El has also got the most loyal customers in the industry (around 80% customer loyalty), and their services are perceived as the best priced in the industry. 75 % of their God El customers have recommended God El to family, friends and colleagues. God El is also Sweden's fastest growing electricity provider, measured in both revenue growth and customer base growth.

God El has since the inception been focused around building a strong "belief-culture", where the employees really believe in the vision of the enterprise and wants to support it through hard work and extra motivation. According to Founder Stefan Krook, the culture in God El is a unique belief-culture of extremely dedicated employees and management. This is reflected in the relatively low wages that God El pays.

## 8.3 VRIO-analysis

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The EQIC-analysis serves as a basis for the VRIO-analysis and helps to identify which resources and capabilities that might be especially important for Me to We Style and God El respectively.

### 8.3.1 Me to We Style

#### **Supplier relations / alliances**

As seen in the EQIC-analysis, Me to We Style has got some very valuable relations to a wide range of suppliers, since the enterprise is able to get deep discounts with many different suppliers. This is rare, very difficult to imitate for competitors of Me to We Style, and this cost efficiency already deeply rooted in the culture. This intangible resource is a competitive advantage for Me to We Style, and has been deployed directly as a consequence of the fourth sector business model.

#### **Employee relations**

Me to We Style gets well-educated, high-quality, highly motivated applicants willing to work for lower-than-industry-average salaries or performance-based only salaries. This is a valuable, rare, difficult to imitate resource, and is exploited by the organization. It is a direct



consequence of the fourth sector business model, and is very likely a competitive advantage for Me to We Style. It could be possible to imitate if competitors chose a similar business model, but until that happens, it is at least a temporary competitive advantage.

### **Business Model**

The fourth sector business model is what enables Me to We Style to achieve many of the things that increases value of its products and decreases cost of its operations. It is clearly valuable in itself, it is a very rare business model in the apparel industry, it is possible that someone will imitate the business model (but not the relationship to Free The Children, and then as a second mover in the industry), and Me to We Style has definitely exploited this business model thoroughly in the first years in business. At worst, this is a temporary competitive advantage, but very likely a sustained competitive advantage due to the close beneficial two-way relationship Me to We Style has with Free The Children, and also because of the first mover advantage this business model gives in the apparel industry.

### **Access to Capital**

Me to We Style has been able to raise the capital needed for its growth, even though this has been modest. In January 2009, Me to We Style's first capital expansion took place, when Participant Media took a 10% stake in the social enterprise (in an agreement that could be described as less demanding than that of a regular private sector investment). Such capital expansion is definitely valuable for Me to We Style, but it is by no means rare that this happens (on the other hand – it happens in the private sector all the time). Access to capital is not difficult to imitate by competitors, but the exact details of the agreement might be difficult to imitate by private sector competitors (an investor will not be that nice with private sector companies). This resource has been exploited by Me to We Style. In total, the access to capital Me to We Style has had so far does not give a competitive advantage – but there has not been a competitive disadvantage either due to the fourth sector business model (something that might come as a surprise). It might get more difficult in later stages when more capital needs to be raised, but until then, this is a competitive parity with the rest of the industry.

Table 8 - The VRIO framework applied on Me to We Style

Resource / Capability	Valuable	Rare	Inimitable	Organizable	Competitive Implications
Supplier Relations	Yes	Yes	Yes	Yes	Sustained CA
Employee Relations	Yes	Yes	Yes/No	Yes	Temporary/Sustained CA
Business Model	Yes	Yes	Yes/No	Yes	Sustained CA
Access to Capital	Yes	No	No/Yes	Yes	Competitive Parity

### 8.3.2 God El

#### Customer Relations

As seen in the EQIC-analysis for God El, the relationship God El has with its customers is truly unique. It has got the best customer service, loyalty, price and recommendation rates in the industry. This is extremely valuable, unique, extremely difficult to imitate and definitely exploited by God El, and a very strong (sustained) competitive advantage. The only difficulty here is for God El to educate new potential customers about the business model, because they have had the problem that people actually don't believe that it is possible / true to have such a powerful business model. God El's fourth sector business model, combined with its low-cost strategy is the direct reason for its powerful customer relations.

#### Employee Relations

God El's employees and leadership are willing to work for less than market salaries, but with a better motivation and performance (as the customer satisfaction/customer loyalty rates show). The culture of God El is developing into something unique because of the attitudes amongst employees and leadership. This is very valuable for God El, it is unique for God El, it is very difficult to imitate for its current competitors, and it is exploited by God El. This is a direct consequence of its fourth sector business model, and very likely another sustained competitive advantage for the electricity provider.

#### Supplier Relations

Same as Me to We Style, God El has also gotten a lot of services and products free or at very low cost from its suppliers, as a direct consequence of the fourth sector business model. This

valuable, unique in the industry, extremely difficult to imitate for existing players and definitely deployed by God El. It is at worst a temporary competitive advantage (until a new player with a similar business model shows up – something that is very unlikely due to the fact that God El has the first mover advantage), but very likely a sustained competitive advantage for God El.

### Access to Capital

Stefan Krook, Founder of God El, thinks that access to capital can be God El's major weakness over time (when more capital is needed for expansion). So far, God El has been able to get 11 million SEK as donated start-up capital, plus several interest-free loans. There has been no major capital expansion yet, but it does not seem like God El has tried either. The explosive growth is financing further growth. On the other hand, the donated start-up capital and interest-free loans that God El has received has been valuable, it is previously unheard of in this industry, it is extremely hard to imitate, and God El has already done it. It can therefore be claimed that God El's access to capital so far has been a competitive advantage, since it helps to substantially lower the financial cost of the enterprise, compared to what another private sector venture in the same industry would have had.

### Business Model

All of the resources above has been possible to exploit mostly because of the fourth sector business model (combined with an innovative cost-only plus small fee product). The fourth sector business model has so far proven valuable and unique to God El. With the first mover advantage, it will be more or less impossible to imitate, and it has been exploited by God El (and will continue to be in the future). Therefore the business model for God El is a sustained competitive advantage.

Table 9 - The VRIO framework applied on God El

Resource / Capability	Valuable	Rare	Inimitable	Organizable	Competitive Implications
Customer Relations	Yes	Yes	Yes	Yes	Sustained CA
Employee Relations	Yes	Yes	Yes	Yes	Sustained CA
Supplier Relations	Yes	Yes	Yes	Yes	Sustained CA
Access to Capital	Yes	Yes	Yes	Yes	Competitive Advantage
Business Model	Yes	Yes	No/Yes	Yes	Sustained CA

## 8.4 Survey Findings

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### 8.4.1 Customers

According to a survey by MORI in the UK in 2002, 86 % of the surveyed said that it is important that a company shows a high degree of social responsibility when they are forming a decision about buying a product or a service from a particular company or organization. One in three have bought a product because an established link to a charitable organization in the past year, while one in six have actively boycotted a product on ethical grounds. One out of four have recommended others to use or avoid products from selected companies based on their degree of social responsibility (MORI, 2002).

In a survey conducted by Carat Insight for UNICEF in Norway in 2005, did 69% reply that they agreed with the following statement: “If I can choose between two equal brands or companies, it is likely that I would choose the one that supports a good cause over the one that doesn’t support a good cause” (Carat Insight, 2005).

These surveys show that there is a great demand in the public for products with a high degree of cause-orientation / social responsibility.

### 8.4.2 Recruiting

In Net Impact’s survey of 2113 MBAs in the U.S and Canada (Net Impact, 2007), 79% percent of students say they will seek socially responsible employment at some point during their career, while 59% say they will do so immediately following business school. Women are significantly more likely to seek socially responsible employment than men.

78% of the surveyed agree that corporate social responsibility is a topic that should be integrated into core curriculum classes at MBA programs, and seventy percent agree that business schools should put more emphasis on such training than they do today. 81% of the students believe that companies should try to work toward the betterment of society.

In the Universum Graduate Survey 2007, a survey amongst graduates in Norway, 24 % replies that a company's social responsibility is the most important criteria for choosing their employer, whereas 28% feels that a high ethical standard is the most important factor. This is the third year in a row that these values are more important than the actual salary, and the conclusion is that the students can afford to focus on self-actualization. This indicates that socially responsible companies can offer lower wages than less socially responsible companies, and still compete for the same candidates (Universum, 2007).

#### 8.4.3 Employees and Wages

A 2004-report by Deloitte & Touche USA LLP showed that 72% of employed Americans – when deciding between two jobs with the same location, responsibilities, pay and benefits – would choose to work for a company that supports charitable causes. 87% of employed students said they would want to work for a company that supports charitable causes. 92% of Americans in general think it is important for companies to make charitable contributions and donate products and/or services to nonprofit organizations in the community. Forty percent of the 3500 respondents to the survey said good corporate citizenship makes them more willing to do business with a company (Fromherz, 2006).

According to a survey by Ipsos Mori in the UK in 2006 (Ipsos MORI, 2006), says 86 % of the respondents that it is very important that their employer is socially and environmentally responsible. 3 out of 4 would recommend a company like this as an employer to a friend or a family member, and 75 % of the people that works for such a company say they have a high commitment to their workplace, compared to 50 % for those who feels they don't work for a responsible company.

The findings above are also supported by Robert Frank in his book "What price the moral high ground" (2004, pp. 77-78) – a morally satisfactory job can be paid 29.5 % less than a regular job, and 43.1 % less than a morally unsatisfactory job. These findings are reliable and valid, as a result of a survey amongst second year MBA-students at Cornell University. This shows that altruistic motives are rather important in economic behavior, and that moral job satisfaction works as a substitute for higher salaries.

## 8.5 Chapter Conclusion

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Based on the strategic analysis in this chapter, combined with survey data, it can look like companies practicing a very high degree of social responsibility plus fourth sector companies might have some advantages when it comes to the trade-off between moral job satisfaction and salaries. Employees of socially responsible companies are also more committed than employees in companies that are not socially responsible, something that very likely will affect company performance over time. It is believed that the commitment and the moral job satisfaction will increase with the degree of social responsibility, and we can see signs from God El and Me to We Style that the moral job satisfaction in these fourth sector companies enables them to pay substantially lower salaries than their competitors.

Customer surveys show that most customers would prefer a product/company that gives to charitable causes over a product/company that doesn't – all things equal. This is very clear in God El, where the relationship they have to their customers is a clear competitive advantage. God El is also Sweden's fastest growing electricity provider, proving that customers are more than willing to support a company with a dual social and financial value creation mission like God El.

The strongest finding in the strategic analysis is the sustained competitive advantage both God El and Me to We Style had in their supplier relations (as a consequence of their fourth sector business model). To be able to get a wide range of products and services for free or at extreme discounts is very unlikely in the industries where the two fourth sector companies operate, and definitely influences the overall operating costs of these organizations in a good way. A lower cost-base leads to higher profitability, and therefore a competitive advantage.

For both fourth sector companies, the access to capital was looked into, since this was one of the major potential weaknesses introduced in chapter 6. It has to be said that both companies analyzed are young start-ups, and there might therefore not be possible to analyze the full extent of their business model. Though, it has to be pointed out that for both companies, the business model has not been preventive for the access to capital so far – on the other hand, it looks like especially God El (and also Me to We Style) actually has access to cheaper capital than its competitors (though for a rather modest capital need). This might change as the capital need increases.

## Chapter 9 – Implications and Conclusion

In this dissertation the new phenomenon of the fourth sector (and the background for its rise) has been thoroughly explained and defined, and there has been conducted a strategic analysis of two fourth sector companies.

It is clear that the phenomenon of the fourth sector is arising as a consequence of many contemporary changes in society, where there is an increased supply and demand for a new, more humanistic version of capitalism, where social and financial value creation goes hand in hand.

From presenting solutions to more social value creation in the private sector, and more financial value creation in the nonprofit sector, the dissertation has criticized the vagueness of many of the existing definitions and tried to contribute with a new, more operationalized definition of the fourth sector. This definition can probably be improved further, but is also a substantial improvement from previous definitions. There is room for improvement to go deeper into the actual operationalization of the definition and start classifying companies with the definition in mind (and hopefully also discuss whether the definition presented makes sense most of the time). Since there is a wide range of organizational models out there in the real world, there might be organizational models that have not been mentioned that should or shouldn't be classified as those of the fourth sector (such as co-operatives, savings banks/institutions, public-private partnerships, religious organizations, investment funds held by associations etc). Hopefully the definition presented can help with the classification of all of these organizational models, at least recognizing that companies with greater, public purpose plays an important role and constitutes a bigger part of the world economy than previously predicted. A direct implication of this definition is for example that companies owned more than 50% by national governments also can be classified as fourth sector companies, something that makes the fourth sector quite much larger than many would have expected.

The Strategic Analysis of the two fourth sector companies God El and Me to We Style had some interesting findings. There is clearly a set of resources and capabilities in these companies that has contributed to the immediate success of these two businesses, much

thanks to their fourth sector business models. If this is scaled up, implications could be that private sector companies have some potential competitive advantages in their relations to their stakeholders – especially when it comes to bringing down the operational cost of these entities. A potential implication is that (first-mover) fourth sector companies can have some systemic competitive advantages compared to their equivalents in the private sector – all other things held equal. But concluding with this would be to speculate, and it is really too soon to say, based on a short analysis of two new ventures. It would be interesting to go further into a wider range of fourth sector companies that communicates their greater good purpose business-model to their stakeholders, and see if there are actual common traits of competitive advantage and/or disadvantage also for more mature fourth sector companies – such as Newman’s Own in the U.S. Is the fourth sector business model prohibiting for business expansion and raising capital in the long run, or will fourth sector companies find ways to get around this? If they do, that could imply that this actually is an entire sector, not just of greater good (altruistic) corporations, but also altruistic, greater good-investors, banks, and support-institutions. This is a field where more research needs to be conducted.

On a global level, a systemic approach to constructing the fourth sector around the definition presented in this dissertation would be highly beneficial for a more direct redistribution of wealth in the world towards those in need. This is not the solution to all the problems in the world, but would definitely be of great help to solve some of the current issues humanity is facing. More fourth sector organizations will arise in the years to come, and with an increased momentum of altruistic entrepreneurs and investors, it is possible to create a fairly powerful sector that is able to raise substantial amounts of capital towards those in need, not to mention the impact these organizations will have on social issues in itself through their core product offerings and core conduct, often as impactful as anything else.

The definition of the fourth sector needs more research to become even better, and it needs to be presented as a new sector in academic institutions all over the world, especially in business studies. Human beings are motivated by more than financial values, and this is mirrored in the purely altruistic and social nonprofit and public sectors. But there should definitely be room for a fourth sector, that celebrates the power of the capitalistic system and long-term profit maximization, that harnesses the power of this brilliant system and combines it with the brilliant altruistic greater, public good purpose of the nonprofit and public sectors. This is the best from two worlds and potentially an extremely powerful combination for positive change.



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# Appendices

## Appendix 1 – New York Times Article

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### Businesses Try to Make Money and Save the World

Stephanie Strom, New York Times - May 6, 2007

ALTRUSHARE SECURITIES is a brokerage firm, engaged in the sort of things you might expect of a Wall Street outfit, like buying and selling stock, and providing research on companies. Unlike its peers, however, the firm is majority-owned by two charities that each control about one-third of it.

So is it a for-profit business? Or a nonprofit fund-raising machine?

In fact, like hundreds of new businesses starting up around the country, it is both. Altrushare is an example of the emerging convergence of for-profit money-making and nonprofit mission.

The practice is even creeping into corporate bluebloods like General Electric, whose \$12 billion Ecomagination business promotes its products' minimal environmental impact as well as their positive impact on the bottom line.

"We're a for-profit institutional brokerage, and we have to compete on execution and commissions and do so with the same technology and talent you would expect from a top-tier firm," said Peter Drasher, a founder of Altrushare, which is based in Bridgeport, Conn. "What makes us different is our nonprofit ownership and our mission, which is to support struggling communities with our profits."

The nonprofit sector is also part of the movement. Motivated by growing competition to attract donor dollars, charities are going beyond longstanding practices. Some are adopting innovative investment strategies or owning other ventures outright.

"I think what people are increasingly looking for, whether in the for-profit or nonprofit sector, is how you harness the vitality and promise of capitalism in a way that's more fair to

everyone,” said Juliana Eades, the president of the New Hampshire Community Loan Fund, a nonprofit mortgage lender that has begun dabbling in other types of financing.

The result is a small but budding practice — what some label the fourth sector — composed of organizations driven by both social purpose and financial promise that fall somewhere between traditional companies and charities. The term “fourth sector” derives from the fact that participants are creating hybrid organizations distinct from those operating in the government, business and nonprofit sectors. But because the types of participants vary widely and much of the activity is nascent, no single name for what is occurring has gained broad use.

“There’s a big movement out there that is not yet recognized as a movement,” said R. Todd Johnson, a lawyer in San Francisco who is working to create an online wiki to engage in the give and take of information for what he calls “for-benefit corporations,” another name for fourth-sector activities.

Consumers, employees, managers and — perhaps most important — investors are driving the phenomenon.

“Young M.B.A. students are not satisfied with going to work for a normal corporation because they are passionate to do good in the world and do it in business,” Mr. Johnson said. “People of faith want exactly the same thing, and there is a whole generation of people who’ve become extraordinarily wealthy as a result of the technological revolution and are now asking themselves if they can create change in the world.”

Those desires are reflected in the growth of so-called sustainable enterprise programs at the nation’s most prestigious business schools, in the corporate marketing campaigns that emphasize social benefits instead of mere sex appeal, and a blossoming of new investment vehicles like Good Capital, Investors’ Circle, Underdog Ventures and the Social Venture Network.

STILL, whatever participants call it, the fourth sector faces challenges. Current legal and tax structures draw strict lines between for-profits and nonprofits, and fiduciary obligations prevent asset managers from making investments with any aim other than maximizing profit. The social benefits that fourth-sector firms seek to unlock are not easily quantified and often take decades, not quarters, to attain.

“You run into fundamental problems in trying to grow good because neither for-profit nor nonprofit is set up to do what new entrepreneurs and others are trying to do — namely, harness the power of private enterprise to create social benefit,” said Jay Coen Gilbert, co-founder of B Lab, a start-up organization based in Philadelphia that will develop what he calls “B corporations,” which engage in fourth-sector pursuits.

Even so, some mainstream companies say it makes sense to give the emerging fourth sector serious consideration. Goldman Sachs, the Wall Street investment bank, has a four-member research team that assesses the environmental, social and management performance of companies in the same way that more traditional colleagues analyze financial performance.

Goldman’s efforts grew out of a report it produced in 2003 for the United Nations Environment Program Finance Initiative. It was asked to come up with ways to measure corporate response to issues ranging from gas emissions to employee health and safety practices and to determine how they related to the companies’ financial performance.

To the firm’s surprise, investors began asking for the report, which it had regarded as a one-time project, and requesting more of them. So far, Goldman has produced similar reports on the media, mining, steel and food and beverage industries. Each week, it sends out an e-mail message on sustainable investing to about 400 contacts at 80 institutions worldwide.

“Integrating factors such as environmental impact and corporate governance is an increasingly critical part of investment research,” said Marc Fox, a research analyst at Goldman. “What began as a niche market of socially responsible investors has expanded to mainstream institutions such as pension funds and insurance companies who seek long-term investment performance.”

In 1993, Mr. Coen Gilbert was a founder of And 1, a \$200-million footwear company based in Paoli, Pa., committed to enriching its employees’ work lives while using its profits to support youth development and educational programs.

Long before the Internet era, And 1 provided a gym, yoga classes and other perks to its employees. It also required suppliers to avoid engaging in sweatshop labor practices and hired an independent auditor to monitor compliance. It contributed 5 percent of its profits to charity, and gave money “even when there weren’t any profits,” Mr. Coen Gilbert said.

And 1 was privately held and thus faced none of the pressure to produce quarterly returns that confront public companies, yet it struggled to maintain socially minded programs as it grew. Another privately held company bought And 1 in 2005 and ended the employee wellness programs and charitable activities.

“Under our corporate documents, we had a single fiduciary responsibility, to maximize return for shareholders, and that’s how we made the decision to sell the company,” Mr. Coen Gilbert says.

Legions of companies that have sought to occupy the middle ground between nonprofit and for-profit have bowed to pressure to sell to conglomerates, including Ben & Jerry’s (sold to Unilever) and the Body Shop (now owned by L’Oréal). Others, most notably Patagonia, have simply refused to sell or to go public.

Similar companies today are evolving in a different environment. Investors, customers and consumers are developing a more holistic approach and focusing on the longer term, attitudes that support changes in the way business is done.

Companies themselves are beginning to understand that what appears to be an expense today may in fact produce lucrative long-term benefits, either by reducing costs or resulting in products and services that can be sold. And investors are increasingly rewarding companies for such actions.

“There are many motivations for this,” said Abby Joseph Cohen, Goldman Sachs’s influential chief United States portfolio strategist. “Companies are taking a broader view that allows them to see that a cost today may reduce future liabilities, and the reduction of those future liabilities in turn has a positive impact on their cost of capital.”

Among major investors, perceptions of profit and value are changing, too. For instance, the California State Teachers’ Retirement System, the \$162 billion pension fund, has taken a hard look at insurance companies. It decided that companies in the industry were not paying enough attention to climate change and thus were a riskier investment than in the past, according to Jack Ehnes, the chief executive of the fund.

“In the past, we’ve created this dichotomy between financial and social, and investors have been ridiculed for placing too much emphasis on social factors,” Mr. Ehnes said. “Maybe that



bright line test is really phony and in fact there has to be a commingling of these factors in investment analysis. If you're really going to be thinking long term about a company's profitability, you'll need a better tool kit for your analysis."

The pension fund holds stakes in wind farms, solar panel manufacturers and developers of low-income housing in its alternative-investments portfolio, and it has assigned a team to assess the impact of factors like environmental stewardship on risk and financial performance across its portfolio.

Funds like the teachers' pension fund are big clients of Wall Street firms, as are many of the wealthy individuals who are looking for opportunities in the fourth sector. By and large, however, investors like those are not looking to invest in companies like the Farmers Diner in Quechee, Vt. — which tend to be extremely risky, no matter how well intentioned they may be.

"Companies like us have no conventional road map to follow in building our businesses and thus are greeted with a lot of skepticism," said Tod Murphy, who founded the diner nine years ago.

Farmers Diner is aiming to build a new food sourcing and distribution model. About 65 percent of its budget for food ingredients is spent within 70 miles of the restaurant, and it tries to educate local farmers about new business practices. The goal is to create a network of four restaurants served by a central kitchen that draws most of its ingredients from the local market.

Making the model work has been difficult, though. The diner's original location, in Barre, Vt., was too small to generate the revenue needed to cover expenses. Banks would not back the venture, and Mr. Murphy's angel investor, a money manager named Cathy Berry, eventually was tapped out.

The diner closed for a year, reopening in a much larger space in Quechee. Mr. Murphy says that it is on track to have more than \$1 million in revenue this year, and that another person has promised to make an investment if the diner can demonstrate consistent profitability.

For her part, Ms. Berry remains enthusiastic about enterprises like the diner; she is on the board of Investors' Circle, one of many organizations working to link investors to hybrid companies.

"What we are constantly coming up against is our tax laws and our culture," Ms. Berry said. "The whole fabric of society wants us to make money on one side and do good with it on the other. What we're saying is: What if we did both things at once?"

She and others argue that current laws, tax structures and definitions of fiduciary responsibility encourage companies to shift costs onto society. "We have created cheap food by investing in huge agricultural conglomerates — but is it really cheap?" she asks. "No. Look at the pesticides those businesses use and then look at the cleanup costs to society. Look at the health costs."

Ms. Berry, Mr. Murphy and others like them want tax breaks to offer incentives that compensate businesses for absorbing the social costs of their activities.

"We want social responsibility to be completely embedded in everything we do, not something that occurs as a sort of sideline," said Heerad Sabeti, co-founder of TransForms, a company started in 2005 in Raleigh, N.C., that makes removable wall decorations. "It has to be an integral part of our business."

Mr. Sabeti says he is tired of advisers who tell him to run TransForms as a purely commercial venture and to simply direct a portion of its profits after the fact to a foundation for distribution to good causes. "What good does that do if I'm using plastic for my packaging and helping to contribute to job losses by manufacturing in China?" he asks.

Mr. Sabeti and his wife, Maja Palej, the chief executive, chose to manufacture their products in the United States rather than in China, despite the higher labor costs, to support jobs here. They also hired a nonprofit group that offers training, education and employment to disabled people to handle packaging.

TransForms, with revenues of almost \$2 million, has financially succeeded, its owners say, in part because it landed a steady client: Bed Bath & Beyond, the housewares company. Thanks to that relationship and new ones with QVC and Target Online, TransForms has not needed

outside investors. But Mr. Sabeti knows that he needs such backing to gain credibility, and he is hoping to attract one or two angel investors to supply \$1 million or more in capital.

HE worries, however, that bringing in investors will force him to compromise his commitment to his principles. “I don’t know that as a for-benefit company, you’re going to spin off the kind of returns venture capital demands, or that you’d want to,” he said.

That’s the reason fourth-sector financiers are so important to the growing movement; they’re willing to invest patient capital that supports businesses that produce both profit and social benefits. For instance, the New Hampshire Community Loan Fund, a 23-year-old nonprofit organization that was one of the first to develop resident-owned mobile home parks, has branched out into a form of venture capital.

In many ways, the loan fund operates under even greater fiduciary constraints than mainstream investment managers. Nonprofits are risk-averse, given their role as stewards of charitable donations, and their tax-exempt status limits what they can do in operating a business.

So, in 2002, when the loan fund wanted to keep alive Bortech, a tiny machine-tools company in Keene, N.H., to preserve jobs, it used an investment structure that combined aspects of equity without giving the fund outright ownership of Bortech. When a founder wanted to sell the company, the loan fund provided a local buyer with a \$500,000, 10-year loan at 9 percent interest; the buyer agreed that the fund would also be paid a percentage of Bortech’s revenues for the next five years.

“Our goal in making this investment was to keep the company from leaving the region, and if we structured the deal to give us a piece of the equity, all we would really be doing was delaying the inevitable because it would have to be sold if we were to realize that value,” says John Hamilton, who oversees the loan fund’s venture financing.

To foster socially minded business practices, the fund also gave the company’s new owner, Leo White, revenue-sharing rebates for reducing Bortech’s environmental impact or for broadly engaging employees in its business.

Today, the loan fund’s investment has been replaced by bank financing, Mr. White’s business has thrived, and Bortech now has 14 employees, twice the number it had when the loan fund

first jumped in. The loan fund itself is tapping a source of capital that many fourth-sector participants would like to see become more available to hybrid businesses — so-called program-related investment.

Most common program-related investments, or P.R.I.'s, are low-interest loans that foundations provide to nonprofits. The Ford Foundation, which helped pioneer the concept in the late 1960s, has some \$170 million in assets sunk into program-related investments in 99 nonprofit groups, including the loan fund.

Ford's average loan is \$2 million, far larger than its average grant, and such investments help nonprofits establish a credit and repayment history that can help them get bank financing in the future.

Investors and others are pushing to expand the use of such loans, perhaps through changes to the tax code that would make them available to businesses as well as nonprofits. Foundations, however, would likely be wary of extending the reach of P.R.I.'s, because they can be risky. For instance, many of the roughly 15 percent of P.R.I.'s that the Ford Foundation has written off went to for-profit businesses run by nonprofits rather than for the operation of the nonprofits, the foundation says.

DESPITE the potential pitfalls, business relationships between for-profit and nonprofit players are increasing. Mr. Drasher, Altrushare's founder, has even commissioned a study of the phenomenon because he was surprised by how many nonprofits have a piece of for-profit businesses.

During a 20-year career as a trader on Wall Street, he grew to appreciate the power that capital markets had to foster and build emerging markets around the world. "I really did see what this industry has done for regional emerging markets, which have become a legitimate and desirable asset class, and I started asking myself, 'Why aren't we doing the same thing for our own emerging markets, our underserved communities?'" Mr. Drasher said.

Many pension funds invest in low-income housing development and other types of real estate in poor neighborhoods, "but communities are about more than real estate," he said. "You're not going to change people's lives by giving them low-income housing alone," he added. "They need job opportunities and education."

Altrushare has created a mentoring and jobs program with the New York Institute of Finance for college students. The goal is to put each student in the program into a paid internship at a Wall Street firm.

Could Altrushare or any other budding hybrid become another G.E.? Perhaps the better question is whether G.E. and other corporate titans could themselves become hybrids.

Shortly after Jeffrey R. Immelt took the helm at G.E., he traveled around the world talking to customers, who asked for energy-efficient technologies, says Peter O'Toole, a G.E. spokesman.

Mr. Immelt committed \$1 billion toward research and development that would reduce the environmental impact of its products — leading to the unveiling in 2005 of Ecomagination, a unit that sells products like the GE90-115B aircraft engine.

“Each year, a fleet of 16 twin-engine aircraft powered by GE90-115B engines will emit 141,000 fewer tons of greenhouse gas emissions than if it used the competing airframe requiring four engines,” the division’s Web site says. “That equals the carbon dioxide absorbed by 35,000 acres of forest, an area twice the size of Manhattan.” Ecomagination products make up more than 7 percent of G.E.’s sales and are expected to produce \$20 billion by 2010.

But G.E. also promotes the engine’s ability to help the customer’s bottom line by increasing fuel efficiency. “This wasn’t something we did to make ourselves feel good,” Mr. O’Toole says. “It has a real business rationale.”

## Appendix 2 – Financial Times Article

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### Social enterprise - the fledgling fourth sector

By Chip Feiss – Senior Fellow, Harvard Kennedy School of Government

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Is it possible that a whole new, distinct fourth sector is developing right before our eyes? The modern business world has up to now comprised the private for profit, public/ government and non-profit sectors. But today there is a blurring of the lines between these sectors. There is also a burgeoning global movement, known as social enterprise, which straddles all the other sectors.

But, first, if social enterprise is to become the new fourth sector it will need to overcome some structural challenges. The first is one of definition. The term "social enterprise" has been imbued with many different meanings and become associated with other catchphrases such as "sustainability", "green" and "corporate social responsibility".

I define it as a for-profit/non-profit or hybrid business, using private investment to work on common-good social problems.

Virtually daily there is news of another social enterprise initiative, as individuals and institutions such as business schools, where courses on social enterprise are among the most popular, explore alternative ways to create financial and social value. Those involved in launching these new enterprises clearly reject Milton Friedman's perspective "that the social responsibility of business is to increase its profits".

Although experiencing a huge upsurge in interest and visibility globally, social enterprise is still in its nascent stages. Today it can be characterised as a fragmented sector filled with many small-scale enterprises struggling with scale. Growth and scalability are important concerns for all businesses but maybe more so for social enterprise, in that the scope of the social problem(s) it is trying to solve is so large.

Innovative work is being done to reach scale, including the development of corporate structures, tax policy that considers the social benefit delivered by social enterprises, the design of systems to measure social value and impact, the creation of social capital markets for improved financing of social enterprises and the development of funding sources and investment instruments.

The establishment of social enterprise as a distinct, flourishing sector faces many challenges, but history is encouraging. Concerns over income inequality, environmental degradation and

social justice have prompted people to search for and experiment with new ways to do business.

The recognition by many people of the failure of business and public policy to deal with these issues adequately has led, among other things, to the global proliferation of non-profit organisations. They have doubled in number in the US alone in the past 15 years.

This same awareness motivated people to align their investments better with their values and gave birth to socially responsible investing, which has also seen dramatic growth. In the UK, funds invested with a socially responsible focus have grown from £1bn to £764bn (\$1,260bn, €897bn) in 12 years. The opportunity for social enterprise is huge. The Monitor Group estimates that this could be a \$500bn-a-year sector within five to 10 years.

There are, of course, those who question the efficacy of social enterprise, including President Barack Obama's economic adviser Larry Summers, who wrote: "It is hard in this world to do well. It is hard to do good. When I hear a claim that an institution is going to do both, I reach for my wallet. You should too."

While I also believe it is hard to do well and/or good, I am encouraged by social enterprise, which appeals to a larger part of the human spirit and experience than some of the traditional business models.

Social enterprise is not meant to replace the other sectors but is another way of dealing with common social problems that have not been successfully addressed to date. Is it possible? When history collides with motivation and opportunity anything is possible.

*Chip Feiss is a senior fellow at the Center for Business and Government at Harvard Kennedy School of Government*

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## Appendix 3 – God El Interview

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Interview with Stefan Krook, Executive Director God El – April 30<sup>th</sup>, 2007

1. *What was your motivation for starting God El?*

- Had started another company earlier (Glocalnet). Knew he was good at both entrepreneurship and business operations. Where at this point in time interested in what made him happy. Realized that he needed enough money (but not much) to cover a moderate personal consumption, and also wanted to do something good for others. Then he thought of how he could combine these two...

- Good Cause as a concept where built first (in 2002/2003). Then he started God El in 2004.

2. *Why did you choose this business model (with 100 % ownership of God El by a charitable foundation, Good Cause)?*

It was all or nothing. 100 % ownership by the charitable foundation gives it the full opportunity to decide everything themselves. With 100 % ownership by the foundation, this is also a structural decision that makes it very difficult to alter.

100 % ownership also gives higher credibility, not necessarily towards customers and employees, but towards strategic alliances. Wouldn't have experienced that much goodwill with e.g. a 50 % ownership.

Wrote his dissertation on company culture and so-called "belief cultures", and knew that there might be advantages with such a business model towards the employees.

The concept (Good Cause – a charitable foundation as 100 % owner of a for-profit company) was decided upon first, almost as a corporate structure and a mother company, like Virgin. They would like to enter different business areas in some time. The business model God El uses can be copied and used in other industries as well – especially when it might give a first-mover advantage. The dream is that Good Cause is a big, international owner/corporation with many different subsidiary companies underneath.

3. *Have you experienced any advantages / disadvantages with this business model?*

The access to financial capital will probably become a great disadvantage over time. They have got enough investment capital in the first phase, but are unsure of what will happen in the second and third capital expansion-phases. They cannot offer investors other returns than social utility from their capital, and thereby the investments can be compared to pure donations, since the investors won't get anything back financially.



God El follows a low cost, low price strategy. This is making them more credible, in Krook's eyes.

Another disadvantage is that God El has to educate many customers, because many of them do not understand their business model, that this is possible. Therefore, they for example send out an informational newsletter with the monthly bills.

An advantage is that they can pay lower wages than their competitors. Krook wants people that work for God El to work there not because of the money, but because they want to help doing good.

God El can make decisions that can give social contributions before profit maximizations, since the main goal anyway is to create positive social change.

4. *Have you experienced any advantages / disadvantages with any of the company's stakeholders because you have this business model?*

**a. Customers**

(+) Gets more customers because of the business model. Gets more loyal customers because of the business model. 75 % of their customers recommend God El to family, friends and colleagues. The customers can themselves choose which good cause their "share" shall go to.

Break even = 25 000 customers. They have got 50 000 customers during their first two years.

(-) Customers have to be educated. Some are very sceptical: Is this really possible?

**b. Employees**

(+) Have the feeling of working towards a common goal of higher purpose. Motivation for everyone, but of course of different degree for the individual employee.

Stefan Krook is sure that the employees are positively affected by the business model. Some employees (e.g. the chief of operations) work there because he was really into the concept.

As mentioned: Can offer lower wages than their competitors.

**c. Owners / Investors**

(+) Have gotten donations when they have had the need for capital.

(-) Not yet in a second expansion phase where capital is needed. God El has no bank loans yet either. Potential disadvantage when more capital is needed.

**d. Government / Regulating Institutions**

N.A.

**e. Media / Surroundings**

Very good deal with Swedish TV4: Result-based payment for commercial – God El will pay according to how many new customers the commercial generates. TV4 has been more risk-willing than one might expect in this case.

Very good media reach in general, more than one could expect.

**f. Suppliers**

N.A.

**g. Other Strategic Alliances**

Has gotten free furniture for the office, free law consultation, free IT-services, free graphical design, and a free commercial as well.

God El has also gotten the possibility to recruit customers inside a big mall (Åhlens) in Stockholm, where no competitors are allowed to have stands.

## Appendix 4 – Kavli Group Interview

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Interview with Erik Volden, CEO, Kavli Group, June 4<sup>th</sup>, 2007

*1. Have you experienced any advantages / disadvantages with this business model?*

This business model gives an additional dimension to many consumers, customers, government, employees. Will not push the business model down the throat on anyone, but will have to be better in branding their product. But only recently the laws changed in Norway, and it is now legal to brand the products with labels such as “100 % of the profit is donated to charitable causes”.

(-) Prerequisite that one will continue operations. Mergers are impossible. Lack of Equity Instruments.

(-) Prerequisite: will have to make at least as good products as the competitors. -> All equal!! Then, the business model might be a point of differentiation. Hardcore business will be combined with doing good, but doing good comes after hardcore business.

2. *Have you experienced any advantages / disadvantages with any of the company's stakeholders because you have this business model?*

**a. Customers and Consumers**

Today, less than 5 % of Kavli's consumers know that they are 100 % owned by a charitable foundation. Kavli wants to enhance this number.

The customers and consumers that knows of this, is very loyal. Those who know about the concept, are vital supporters for Kavli.

There are two ways to sell the products:

- 1) Sell the products because they can support good causes
- 2) Tell so much about the good things you do that you sell more products. The latter, is according to Mr. Volden, a more pure way to do it.

**b. Employees**

Easier to build a good company culture with this business model. Should not be a wage leader, even though the incentive systems will have to be competitive. The business model is something the employees are proud of.

**c. Owners / Investors**

Good governance is extremely important, since they are 100 % owned by a charitable foundation. 12-13 years ago, there were problems in the communication between the company and the owning foundation, and therefore a holding company was made.

It is vital that the owners and the general assembly have got the power to fire the CEO if they feel this is needed. It is also vital that the owners behave as good, rational owners. A business model like this is easier to take advantage of than a ordinary for-profit company where the owner-incentives are much stronger.

Some of the earlier CEOs did too much. Took too much risk, made decisions of poor quality, invested in unrealistic companies (because of insufficient owner control – classical principal-agent problem).

Administration of the foundation: The administrator have to be an outgoing and active person. Both the company and the foundation should be open and easy accessible. The foundation will also have to be concerned about it's reputation. Since Kavli is an international corporation, the foundation will also have to do some good in the other countries where Kavli operates.

Kavli has bank loans, as everybody else.

**d. Government / Regulating Institutions**

In a discussion with the public authorities about general framework, Kavli has used their ownership structure, and gained advantages because of this.

**e. Media / Surroundings**

A lot of positive attention with Q-Milk, but more attached to Q-Milk as a small challenger.

**f. Suppliers**

Not price-advantages, but many suppliers like to work with Kavli because of the business model, such as PR-bureau's and ad-agencies.

**g. Other Strategic Alliances**

N.A.